The Choice-of-Law Methodology Applied in ICC and CIETAC Arbitration

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Tiivistelmä/Referat – Abstract

Tämä tutkielma systematisoi, vertailee sekä analysoi Kansainvälisen Kauppakamarin ("ICC") sekä Kiinan kansainvälisen välimiesmenettelykeskuksen ("CIETAC") välimiesmenettelyssä sovellettavaa lainvalintametologiaa. Toisin sanoen, tutkielma pääasiallisesti käsittelee ICC:n ja CIETAC:n välimiesten käyttämää menetelmää sopimukseen sovellettavan lain määrittämiseksi sopijapuolten tekemän (nimenomaisen tai hiljaisen) lakiviittauksen puuttuessa. Huolimatta sekä ICC:n että CIETAC:n keskeisestä merkityksestä modernissa kansainvälisessä välimiesmenettelyssä, välimiehet joutuvat ko. välitystuomioistuimissa sopijapuolten antamien ohjeiden puuttuessa käyttämään huomattavan erilaisen harkintavallan antavaa lähestymistapaa sopimukseen sovellettavan lain määrittämiseksi. Käytännössä tämä tarkoittaa sitä, että kansainvälisessä välimiesmenettelyssä nykyään korostetussa asemassa oleva sopijapuolten tahdonautonomian periaate toteutuu verrattuna esimerkiksi ICC:n välimiesmenettelyyn CIETAC:n välimiesmenettelyssä poikkeuksellisen heikosti. Ottaen huomioon Kiinan kansantasavallan keskeinen asema kansainvälisessä kaupassa ja taloudessa, mainitut huomiot tekevät aihetta koskevan tutkimuksen sekä ajankohtaiseksi että kiinnostavaksi.

Kansainvälinen välimiesmenettely ymmärretään nykyään yleisesti kansallisesta laista riippumattomaksi riidanratkaisumuodoksi. Tutkielma kysyykin täten, miksi ja miten kuvattu tilanne on mahdollinen. Erotuksena ylikansalliseen sekä perustamisestaan lähtien kansainvälisen kaupan edistämiseksi toimineeseen ICC:iin, CIETAC on kiinalaisten oikeustieteilijöiden mukaan (ainakin muodollisesti) sosialistisen yksipuoluevaltion alueella toimiva valtiosta riippumaton organisaatio. Voiko tällainen toteamus ensinnäkään pitää paikkansa? Viimeaikainen Kiinaa koskeva oikeustieteellinen tutkimus on osoittanut, että länsimaisilla Kiinan-tutkijoilla on ollut tapana syyllistyä perusteettomiin ennakko-oletuksiin Kiinasta sekä kiinalaisesta oikeuskulttuurista. Jotta tämä tutkielma olisikin toteutettu mielekkäällä ja objektiivisella tavalla, tutkielma selvittää Kiinan kansantasavallan yhteiskunnan muutosvaihetta reaalisosialismista 'sosialistiseen markkinatalouteen', maan samanaikaista oikeusjärjestelmän kehitystä sekä arvioi maan taloudellisen ja oikeudellisen 'siirtymävaiheen' merkitystä CIETAC:ssa käytävälle välimiesmenettelyprosessille.

Tutkielma osoittaa mainittujen eroavaisuuksien pohjimmiltaan johtuvan ICC:n sekä CIETAC:n välimiesmenettelyssä sovellettavasta välimiesmenettelylaista (*lex arbitri*). Vaikka useat läntiset oikeustieteilijät, välimiehet sekä yritysjuristit pitävät nykyään nk. delokalisaatioteoriaan perustuvia välimiesmenettelyprosesseja oikeutetusti lähtökohtana, Kiina ei edelleenkään ole implementoinut YK:n välimiesmenettelyä koskevaa mallilakia vaan sen sijaan edellyttää nk. perinteiseen näkemykseen nojautuen mm. oman kansallisen lainvalintastatuuttinsa soveltamista Kiinan kansantasavallan alueella pidettävissä välimiesmenettelyprosesseissa. Toisin sanoen, Kiinan kansantasavallan välimiesmenettelylaki asettaa esteen modernisoida CIETAC:in välimiesmenettelyssä sovellettavaa lainvalintamenetelmää.

Lisäksi tutkielma arvioi ICC:n ja CIETAC:n lainvalintasääntöjä koskevan systematisoinnin ja oikeusvertailun avulla näiden mielekkyyttä välityspaikkana eritoten kansainvälisyksityisoikeudellisesta näkökulmasta. Vaikka ICC on sopijapuolten tahdonautonomian periaatteen toteutumisen kannalta näistä kahdesta välitysinstituutista se mielekkäämpi vaihtoehto, tutkielma pyrkii osoittamaan myös tilanteet, joissa CIETAC on ICC:n verrattuna varteenotettava vaihtoehto kiinalaisen sekä ulkomaalaisen partin välisessä riidanratkaisussa. Analyysin syventämiseksi tutkielmassa on perehdytty myös sopimukseen sovellettavan lain merkitykseen riidan lopputuloksen kannalta, CIETAC:n lainvalintametodologiaa koskeviin mahdollisiin oikaisukeinoihin sekä pyritty tunnistamaan merkittävimmät ns. 'väärän' lain valintaa koskevat oikeudelliset riskit.

Tutkielma päätyy suosittamaan Kiinan kansantasavallan välimiesmenettelylain uusimista mm. CIETAC:ssa sovellettavan lainvalintametodologian modernisoimiseksi. Koska Kiinan puolue-valtion pyrkimys kontrolloida alueellaan tapahtuvien välimiesmenettelyprosessien kulkua vaikuttaa kuitenkin olevan CIETAC:n omien instutitionaalisten haasteiden sijasta se keskeinen tekijä, joka viimekätisesti määrittää kiinalaisen välimiesmenettelyn 'erityispiirteitä', kuvatun lainmuutoksen toteutuminen lienee toistaiseksi epätodennäköistä.

Avainsanat – Nyckelord – Keywords

kansainvälinen yksityisoikeus, private international law, lainvalinta, choice of law, kansainvälinen välimiesmenettely, international arbitration, oikeusvertailu, comparative law, ICC arbitration, CIETAC arbitration

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Abbreviations

AAA	American Arbitration Association
Art.	Article(s)
BAC	Beijing Arbitration Commission
BC	Before Christ
CAL	The Arbitration Law of the People's Republic of China
CIETAC	China Economic and Trade Arbitration Commission
CIETAC Rules	China Economic and Trade Arbitration Commission Rules of Arbitration
CCP	Chinese Communist Party
CCPIT	China Council for the Promotion of International Trade
CCOIC	China Chamber of International Commerce
CISG	The United Nations Convention on Contracts for the International Sale of Goods
CMAC	China Maritime Arbitration Commission
COMI	University of Helsinki Conflict Management Institute
CPL	The Civil Procedure Code of the People's Republic of China
EU	European Union
et al.	et alia (and others)
e.g.	exemplia gratia (for example)
FDI	Foreign Direct Investment
FECL	Foreign Economic Contract Law
FIE	Foreign-Invested Enterprise
fn.	footnote(s)
FTAC	Foreign Trade Arbitration Commission
FETAC	Foreign Economic and Trade Arbitration Commission
HKIAC	Hong Kong International Arbitration Centre
GPCL	General Principles of the Civil Law of the People's Republic of China
IBA	International Bar Association
ICC	International Chamber of Commerce
ICC Rules	International Chamber of Commerce Rules of Arbitration and ADR
ICDR	The International Centre of Dispute Resolution
ICSID	International Centre for Settlement of Investment Disputes
LCIA	London Court of Arbitration
ibid.	ibidem (in the same place)
i.e.	id est (that is)
IIL	Institute of International Law
ML	The UNCITRAL Model Law on International Commercial Arbitration
MOFCOM	Ministry of Commerce of the People's Republic of China
NCPC	French New Code of Civil Procedure
No.	number(s)
NPC	National People's Congress
PRC	People's Republic of China
SAR	Special Administrative Regime
SIAC	Singapore International Arbitration Centre
SPC	Supreme People's Court
SC	State Council of the People's Republic of China
SCC	Stockholm Chamber of Commerce
UNCITRAL	United Nations Commission on International Trade Law
WTO	World Trade Organisation

1 Preface

1.1 Introduction to the Subject Matter

The principle of party autonomy (*l'autonomie de la volonté*) is one of the most celebrated features of contemporary international arbitration. The notion of party autonomy refers to the parties' power to determine the form, structure, system and other details of the arbitration. For instance, the parties' agreement to arbitrate, the subject matter of the arbitration and the method of conducting arbitration all are choices made by the parties and thus manifestations of the will of the parties.[1] As procedural flexibility of arbitration is a perceived advantage compared to procedures in national courts, the principle of party autonomy has been assessed to enjoy, in comparison to national courts, particular significance in international commercial arbitration.[2]

As the arbitral tribunal operates on the parties' mandate, the arbitrators are perceived responsible for determining the law governing the merits of the dispute in the absence of the parties' agreement. In performing this task, the arbitrators today generally enjoy broad discretion, which applies not only to the method they use, but also to the subject matter of their choice.[3]

Derived from the parties' power to make procedural decisions regarding the arbitration, the arbitrators' procedural powers may be roughly divided into three major subcategories.[4] These include:

a) jurisdictional power, i.e. the arbitral tribunals' power to decide upon its own competence;[5]
b) choice-of-law power, i.e. the arbitral tribunals' power to decide upon the applicable law to the merits of the dispute;[6] and

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[1] See Redfern – Hunter 2009, pp. 18 – 19 and Lew *et al.* 2003, p. 31.
[2] See Born 2009, pp. 81 – 83.
[3] See Fouchard – Gaillard – Goldman 1999, p. 865.
[4] While this division does cover the main aspects of the arbitrators' powers, it is not, however, exhaustive. Common powers of arbitral tribunals also include the power to decide upon the language of the arbitration, document production, the presence of witnesses, administer oaths and to examine the subject matter of the dispute. See Redfern – Hunter 2009, pp. 316 – 325.
[5] The doctrine of separability (*Kompetenz – Kompetenz*) is an internationally established practice that has gained support and recognition in virtually all modern international and institutional rules of arbitration around the world. Ibid, pp. 346 – 348. It should be noted that China remains an exception to this rule. See Tao 2012a, pp. 95 – 96.
[6] The law, or the relevant legal rules, governing the substantive issues in dispute are synonymously referred to in this study as the 'applicable law', the 'governing law', or 'the substantive law'. See Redfern – Hunter 2009, p. 164.

c) the power to issue interim or conservatory measures, i.e. the arbitral tribunals' power to issue orders intended to preserve evidence, to protect assets, or in some other way to maintain the status quo pending the outcome of the arbitration proceedings themselves.[7]

The pronounced status of party autonomy in contemporary international arbitration owes much to the New York Convention, which stipulates upon the recognition and enforcement of foreign arbitral awards.[8] The New York Convention provides only limited grounds for the refusal of a foreign arbitral award that, in turn, has functioned to further the principle of party autonomy in international arbitration.[9] Additionally, contemporary arbitration laws of virtually all developed jurisdictions feature a similar permissive approach, thus allowing for the parties and their chosen arbitrators to exercise their discretion with no or only little limitations.[10]

In practice, the details of the arbitration procedure are typically left to be governed by the rules of arbitration of the chosen arbitral institution. The parties' power to decide upon details of the arbitral procedure may, however, be limited by the mandatory requirements of the law of the seat of the arbitration (*lex arbitri*).[11] The choice of the place of arbitration strongly contributes to the choice of the law of the seat of arbitration, which governs the existence and the procedural aspects of the arbitration.[12] This being said it is generally accepted that mandatory rules of the *lex arbitri* may typically only be used to ensure that the choice of law is *bona fide* and is not contrary to public policy, resulting in a limited scope of application.[13]

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[7] Ibid, pp. 320 – 323.

[8] As of 2013, a total of 149 countries have ratified the New York Convention. See http://www.newyorkconvention.org/contracting-states/list-of-contracting-states for an up-to-date list of the Contracting States. Last visited 19th of January 2014.

[9] The New York Convention *inter alia* prevents national courts from reviewing the merits of the disputes of the rendered arbitral award. See Fouchard – Gaillard – Goldman 1999, p. 982 and Lew *et al*. 2003, pp. 20 – 21.

[10] The referred development is a result of the UNCITRAL Model Law, which is a means to modernise and harmonise the arbitration legislation of national states. Most states in Europe, North America and parts of Asia have implemented either the Model Law or similar type of legislation to regulate arbitration. See Fouchard – Gaillard – Goldman 1999, p. 69; Lew *et al.* 2003, p. 412 and Saarikivi 2008, p. 40.

[11] See Born 2009, p. 1748.

[12] The concept that an arbitration is governed by the law of the place in which it is held, which is the 'seat' (or '*forum*' or '*locus arbitri*') of the arbitration, is well established in both theory and practice of international arbitration. See Redfern – Hunter 2009, pp. 179 – 183. Should the applicable rules of arbitration allow for it, it is also possible to choose a "foreign" procedural law as the *lex arbitri*. Regarding ICC and CIETAC arbitration, see *infra* Chapters 4.1.1 and 4.2.1.

[13] See Redfern – Hunter 2009, pp. 196 – 197.

The support of the *lex arbitri* may not only be needed to supplement the possible normative gaps in the applicable rules of arbitration but also to give the force of law to orders of the arbitral tribunal that reach beyond the parties themselves.[14] Most importantly, the *lex arbitri* will confer the nationality of the award rendered by the arbitral tribunal, which plays a significant role regarding the enforceability of the rendered award.[15] In arbitration proceedings operated under the arbitration rules of the International Chamber of Commerce ("ICC"), the choice of the place of arbitration could also contribute to the choice of location where the parties are typically, though not bound, to be heard, and the selection of the president/sole arbitrator.[16]

Whereas most contemporary national arbitration laws are permissive and thus allow the parties a wide degree of discretion concerning how their arbitration should be organised and conducted, exceptions to the rule of thumb remain to exist. The People's Republic of China ("PRC") features a unique and, from the perspective of a Western jurist, peculiar arbitration regime. Chinese law not only provides separate categories for the treatment of the arbitral awards but also *de facto* imposes significant limits to the parties' and their chosen arbitrators' autonomy to decide upon the details of the arbitration. While China is, at least in the level of rhetorics, striving to demonstrate its capability and improve its reputation as an "arbitration-friendly" country,[17] the arbitrators relatively limited powers to decide upon the arbitral process under the arbitration rules of China's prime arbitral institution, the China International Economic and Trade Arbitration Commission ("CIETAC"), would *prima facie* appear to lead to the opposite conclusion.

1.2 Subject of Study and Study Outline

This study systematises, compares and analyses the choice-of-law methodology[18] applied in ICC and CIETAC arbitration. In other words, the study focuses on the methodology of the arbitral

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[14] For instance, the assistance of national courts is typically needed when the arbitral tribunal wishes to impose interim measures on one of the parties or when the other party is forced to seek the enforcement of the rendered arbitral award on the losing party. See Redfern – Hunter 2009, pp. 439 – 464.

[15] As the New York Convention only regulates the recognition and enforceability of foreign arbitral awards, purely domestic awards are not included in its scope of application. See *infra* fn. 70.

[16] See Grierson – Van Hooft, pp. 112 – 118.

[17] See Arnavas – Gaitskell 2012, p. 1 and Chi 2011, p. 260.

[18] Saarikivi distinguishes the difference between notions 'rule' and 'method' as follows: whereas referring to a conflict rule means a reference to a certain provision that provides the arbitral tribunal with direct and simple rule to determine the substantive law, a method is something more abstract; it provides the means or the framework to determine the substantive law instead of a mechanical approach. See Saarikivi 2008, pp. 58 – 59. Based on this distinction, the notion 'choice-of-law methodology' used in this study refers to the reasoning of the arbitral tribunal to determine of the

tribunal to determine the law applicable to the merits of the dispute in the absence of the parties' instructions under the arbitration rules of the ICC and CIETAC. Notwithstanding the two institutions' substantial significance in contemporary international commercial arbitration, ICC- and CIETAC-administered arbitrations feature distinctly different approaches in this regard, resulting in a vastly different scope of choice-of-law power provided for the chosen arbitral tribunal. As contemporary international arbitration is perceived as an autonomous and delocalised method of dispute resolution, the natural inclination is to ask why and how is this possible.

The study begins by discussing the development of the theory of private international law applied in international commercial arbitration. Most arbitration scholars, practitioners and parties to arbitration today favour a delocalised approach to international commercial arbitration. As critics of the delocalised approach have aptly noted, arbitrations do not, however, operate in vacuums but the territories of national states. Although the harmonisation work with regard to international commercial arbitration has managed to 'delocalise' such proceedings significantly, exceptions may continue to exist. China's national law on arbitration does not allow separate choice-of-law rules for arbitration but instead directs the arbitral tribunal to apply the private international law of the PRC. Such a choice-of-law methodology reflects the traditional approach of private international law. In other words, the study will indicate that the CIETAC's incapability to modernise its choice-of-law rules is ultimately a result of the restrictive Chinese arbitration law.[19]

Nevertheless, why has the Chinese Communist Party decided to abstain from the revision of the choice-of-law methodology applied in CIETAC arbitration? After the end of Maoist rule, the CCP's incentive to build a judicial system has probably related to the Weberian-North thesis regarding the necessity of law for sustainable economic development. Therefore, the Party's failure to reform the CAL has possibly to do with its efforts to seal its political legitimacy amongst the Chinese citizens and, alas, reluctance to give up its control on the Chinese society. In correspondence, the study discusses China's ongoing transition to a society governed by a rule of law and its implications to CIETAC arbitration.[20]

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substantive law as a whole, beginning from the mandate of the arbitral tribunal to choose the choice-of-law rules applied to the merits of the dispute.

[19] See *infra* Chapter 2.

[20] See *infra* Chapter 3.

Furthermore, the study provides a systematisation and functionalist comparison of the choice-of-law rules applied in both ICC and CIETAC arbitration.[21] Premised on the said comparison, the study attempts to analyse the rationality between the choice between the said institutions as an effective and fair method of commercial dispute resolution. The analysis is executed primarily from the perspective of private international law and the principle of party autonomy as a criterion of assessment. In addition, the analysis discusses the significance of the substantive law with regard to the outcome of a dispute, whether effective remedies to enhance the arbitrators' choice-of-law power in CIETAC arbitration exist, and pinpoints the most important legal risks that relate to the application of a "wrong" law in Sino-foreign dispute resolution.[22] The author has considered such discussions necessary so that a more thorough and objective analysis of the subject matter of the study may be provided.[23] Finally, the results of the study are summarised.[24]

Issues of private international law thus are the focal point of interest of this study. Most China-specific academic literature and commentaries regarding arbitration seem to focus on the inadequate enforcement of arbitral awards in People's Republic of China.[25] This tendency has apparently left the scrutiny of choice-of-law issues related to Sino-foreign dispute resolution for only little attention. The point of view of this study will be that of a party counsel pondering whether it is preferable to opt for either ICC or CIETAC arbitration as a method of dispute resolution in an agreement featuring Sino-foreign parties.

Albeit other internationally renowned arbitral institutions of significant importance[26] and specific mandates[27] do exist, this study only discusses the choice-of-law methodology applied under the

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[21] See *infra* Chapter 4.
[22] See *infra* Chapter 5.
[23] See *infra* Chapter 1.3.
[24] See *infra* Chapter 6.
[25] See Cohen 2006, p. 32. In addition to the scholarly writing regarding the enforcement of arbitral awards in China, the issues related to the validity and form of an arbitration agreement and the arbitrability of a dispute have received a lot of attention. See, for instance, Tao 2012a, pp. 177 – 194. WunschARB offers arguably the most extensive database of translated Chinese court decision summaries on arbitration. The summaries published to date have focused on the enforcement of arbitral awards, validity of arbitration clauses and annulment of arbitral awards. See Taylor 2013, p. 1.
[26] For instance, the American Arbitration Association ("AAA"), the London Court of International Arbitration ("LCIA"), the Stockholm Chamber of Commerce ("SCC"), the Hong Kong International Arbitration Centre ("HKIAC") and the Singapore International Arbitration Centre ("SIAC") represent some of the other more famous arbitration centres. See Lew *et al.* 2003, pp. 38 – 39. Of these institutions, at least the SCC, SIAC and HKIAC have been frequently used as forums for Sino-foreign arbitration. See Zimmerman 2010, p. 24 and Håkansson 1999, pp. 52 – 53. At least the Beijing Arbitration Commission ("BAC") deserves a remark from the other more prominent Chinese arbitration commissions. See BAC Official Website, http://www.bjac.org.cn/en/.

arbitration rules of the ICC and the CIETAC. There are several reasons to this approach. Firstly, the ICC Rules may rightly be assumed to represent the latest trends in international arbitration.[28] Secondly, despite the effect of the confidential nature of arbitral proceedings, the amount of available information of institutional arbitration in comparison to *ad hoc* arbitration is far greater.[29] Thirdly, *ad hoc* arbitration inside mainland China is *de facto* forbidden due to the restrictive national arbitration law of the PRC.[30] Fourthly, the ICC and CIETAC Rules have been recently revised, both of them having their latest amendments made in 2012. Last, but not least, the seemingly ever-growing importance of Chinese businesses in international commerce makes an inquiry to the arbitration rules of some of the most popular Sino-foreign out-of-court dispute resolution mechanisms both a fascinating and hot topic.[31]

Partially owing to the same limitations, the researcher has been forced to outline the subject matter of this study to only to cover the implications arising from the scope of choice-of-law power conferred to the arbitral tribunal premised upon submitting to either ICC or CIETAC arbitration. This means the systematisation made in this research is conducted under the presumption the parties wishing to arbitrate have in their underlying contract included a valid arbitration clause that respectively refers to either ICC or CIETAC arbitration without an express or tacit choice regarding the substantive law.[32]

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[27] The China Maritime Arbitration Commission ("CMAC") also handles foreign-related arbitration cases, although it has a much more limited mandate than the CIETAC as it only deals with maritime-related disputes. See CMAC Official Website, http://www.cmac-sh.org/en/home.asp. Legal investment disputes may be submitted to the International Centre for Settlement of Investment Disputes ("ICSID") provided that the contracting parties, i.e. an investor and a state, are situated in different countries that both are members to the Washington Convention. See Lew *et al.* 2003, p. 40 and ICSID Official Website. https://icsid.worldbank.org/ICSID/Index.jsp. Both maritime and legal investment disputes fall out of the scope of this research.

[28] See *infra* Chapter 5.2.

[29] See Born 2009, pp. 2250 – 2253 and Lew *et al.* 2003, p. 283. Saarikivi suggests that the lack of published arbitral awards is, with the exception of ICC awards, the most problematic issue with regard to research on arbitration. See Saarikivi 2008, p. 38.

[30] Article 16 of the CAL requires that an arbitration agreement must contain a chosen "arbitration commission". See Zesch 2012, p. 286. Although *ad hoc* arbitration in China is thus legally impossible, *ad hoc* arbitration awards rendered in foreign countries can still be sought recognition and enforcement in China through the New York Convention. See Tao 2012b, pp. 812 – 813. Gu suggests that the denial of *ad hoc* arbitration in the PRC is a result of the institutional adherence rooted in the Chinese society. See Gu 2013, pp. 88 – 89 and Gu 2008, p. 125.

[31] In the words of Chen, business executives tend to claim that "in terms of business you are either in China or you are nowhere". Although an exaggeration, such a remark aptly illustrates China's increasing importance in the world's economy. See Chen 2008, p. 621.

[32] In the absence of an express choice of law, the arbitral tribunal will usually look first for the law that the parties are presumed to have intended to choose. This is called a tacit or implied choice of law. As virtually no modern arbitration statute contains requirements as to the form of the parties' consent, there is nothing to prevent the arbitrators from

Because of the rigid relationship between the CIETAC Rules and the Chinese Arbitration Law ("CAL"), the inclusion of introductory subchapters regarding the determination of the place of arbitration and the scope of provided party autonomy in both ICC and CIETAC arbitration have been considered as appropriate.[33] The Chinese 'dual-track' system of arbitration and China's multi-jurisdictionality forces to make additional distinctions; this study will only elaborate disputes arising from 'foreign-related' or 'foreign' contracts in the sense meant by Chinese law and only concern the application of the CIETAC Rules in CIETAC venues located in mainland China.[34]

1.3 Methodology and Sources

As this study describes the arbitrators' technique of reasoning to determine the substantive law in ICC and CIETAC arbitration, the methodological approach of the study would *prima facie* appear to be a straightforward systematisation and, to a lesser extent, interpretation regarding the normative content of the arbitration rules applied in ICC and CIETAC arbitration. Despite contemporary international arbitration is consensually perceived as an independent branch of law,[35] CIETAC-administered arbitrations by default apply the choice-of-law rules of the law of the seat of the arbitration, i.e. PRC law.[36] This observation complicates the undertaking to a completely new level. Chinese law is, in essence, of a foreign origin to the author of this study; its eccentric normative hierarchy, a legal language with semantic meanings of its own and China's transitional phase to a society governed by rule of law are, to name a few, such characteristics that continue to cause angst

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inferring from the conduct of the parties that there is an implied agreement as to the applicable law where, for example, the parties argue their case on the basis of the same law, even though they have not expressly agreed to apply it. Should there be any doubt regarding the intention of the parties, the arbitral tribunal may not infer the substantive law. See Redfern – Hunter 2009, p. 230, Lew *et al.* 2003, p. 411; Fouchard – Gaillard – Goldman 1999, pp. 786 – 787 and Lando 1991, pp. 134 – 136.

[33] Because the *lex arbitri* strongly influences the determination of the substantive law under the CIETAC Rules, without the explication of this framework the comparison between the choice-of-law methodology featured in ICC and CIETAC arbitration would be incomplete. As in the case of the substantive law, these subchapters are also conducted with the more common presumption that the parties have not made an explicit choice regarding the place of arbitration. See *infra* Chapters 4.1.1, 4.1.2, 4.2.1 and 4.2.2 and Várady – Barceló – von Mehren 1999, p. 631.

[34] See *infra* Chapter 1.4.1. Chinese law does not allow for purely domestic, i.e. Chinese, parties to choose a foreign law to govern a contract between them. See Liang 2012, p. 80.

[35] In Trakman's words, this consensus can be referred to as the "legal tradition of international commercial arbitration". He does not, however, claim that differences regarding between arbitral institutions around the world would not exist. Instead, whereas ICC arbitration is characterised by a reliance on written testimonies, CIETAC arbitration features a stronger emphasis on oral proceedings and conciliation. See Trakman 2006, pp. 18 – 23.

[36] See *infra* Chapter 2.2.

for foreign legal scholars and practitioners interested in conducting an inquiry to the normative content of Chinese law to date.[37]

The description regarding the application of the Chinese choice-of-law rules could thus be described, in essence, as an idealistic one. The author suggests that the conclusions regarding the application of the Chinese choice-of-law rules should be treated with a certain level of cautiousness.[38] This observation should not, however, pose an obstacle to conduct research into CIETAC arbitration in the first place. The objective of this study is to analyse whether submitting to either ICC or CIETAC arbitration is rational from the perspective of private international law. Should such an undertaking succeed even to the limited sphere attempted in this study, the description is attempted to conduct in a manner that acknowledges the present uncertainties of the Chinese legal system as well as possible, mostly drawing from the experiences of foreign legal scholars with similar ambitions.[39]

The source material of this study consists of literature, commentaries and case summaries prepared by some of the most renowned scholars and practitioners accustomed to both ICC and CIETAC arbitration. In addition, statistics, surveys and charts are provided in order to achieve a more qualified systematisation of the ICC and CIETAC choice-of-law rules. Generally speaking, the requirement of confidentiality[40] set for the arbitration proceedings limits the possibility to conduct any case studies concerning arbitral practice. Whereas an abundance of recent case summaries and descriptions regarding arbitral awards rendered in ICC arbitration is available, relevant arbitral awards issued by the CIETAC are relatively hard to come by. In consequence, the author has been forced to resort to second-hand case summaries of CIETAC awards, resulting in a somewhat anecdotal level of scrutiny.[41] The same is true concerning the availability of statistical data. As an

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[37] See Seppänen 2005a, pp. 3 – 12 and 16 and Peerenboom 2002, p. 21. For a more thorough analysis of China's legal system and its implications to CIETAC arbitration, see *infra* Chapter 3.2.
[38] See *infra* Chapter 4.2.3.
[39] Clarke has pointed out that a research describing Chinese law in the same manner as, for instance, French law would be guilty of "naive ignorance". See Clarke 2003, pp. 93 and also Seppänen 2005a, pp. 16 – 17.
[40] Contrary to proceedings occurring in courts of law, the requirement of confidentiality refers to the parties' desire to keep the content, outcome and even the existence of the dispute in secrecy *ultra partes* in order to, for example, avoid damages to the commercial reputation of the parties. See Cordero-Moss 1999, pp. 150 – 151.
[41] The CIETAC awards cited in this study consist of translated case summaries published by Unilex and Pace Law School. Consequently, they are primarily related to the application of the CISG. See http://www.unilex.info; http://www.cisg.law.pace.edu/. Kluwer Law International does currently publish a non-extensive list of Chinese court decision summaries related to arbitration; most of the relevant decisions concern the enforcement of arbitral awards rendered by the CIETAC. Available at http://www.kluwerarbitration.com/CommonUI/chinese-case-summaries.aspx.

often-cited researcher of Chinese law has aptly summarised, conducting empirical studies is often hard and, in the case of China, "extremely difficult".[42] As an attempt to address the existing issues with China's judicial transparency, the Supreme People's Court of the PRC has recently begun to publish Chinese court decisions on its website.[43] To date, these publications are non-comprehensive and only available in Chinese.[44]

Another challenge is evidently posed by language issues, again, concerning Chinese law. The direct references of this study to Chinese laws or other notions are referred to in Mandarin using the phonetic *pinyin* spelling-technique. The researcher has mostly resorted to the use of qualified translations regarding Chinese laws, regulations and arbitral practice in order to ensure that the semantic meanings of the source material used are as close to the official and hence prevailing Chinese versions as possible. However, it goes without saying that such an approach does have its drawbacks, as it further impedes the author of conducting proper interpretative work with regard to the normative content of the Chinese choice-of-law rules.

Finally, the Chinese rules of private international law seem to currently be in a state of flux. The method applied under the Chinese choice-of-law rules, premised upon the closest connection test, has been strongly relying on the application of presumptory rules. Several Chinese commentators have referred to a judicial document called the 'Rules of the Supreme People's Court on the Relevant Issues Concerning the Application of Law in Hearing Foreign-Related Contractual Dispute Cases in Civil and Commercial Matters' ("SPC Interpretation 2007") as the source of these presumptory rules to date.[45] After the introduction of the new Chinese conflicts statute, the 'Law of the People's Republic of China on Foreign-related Civil Relationships' ("LAL") in 2010, the normative status of SPC Interpretation 2007 document has been under controversy and, as of April 2013, formally abolished. As the newer "Interpretation of the Supreme People's Court on Several

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Last visited November 26th of 2013. Albeit Westlaw International does have a database of CIETAC awards, the majority of the available awards date back to the 1990s and thus represent somewhat outdated arbitral practice. See http://international.westlaw.com. Even Chinalawinfo.com, the most popular legal database in China, publishes only translations of arbitration-related laws, rules and regulations. See http://www.chinalawinfo.com and Luo 2006, pp. 186 – 187.

[42] Even if the Chinese authorities would publish such data, the validity of such data could be considered dubious. See Peerenboom 2001, p. 7.

[43] See http://news.xinhuanet.com/english/china/2013-11/28/c_132926458.htm. Last visited 13th of January 2014.

[44] See http://www.court.gov.cn/zgcpwsw/.

[45] Despite its ambiguity as a source of law already before its formal abolishment, the SPC Interpretation 2007 has been referred to in virtually all earlier studies of Chinese private international law because of the lack of other detailed choice-of-law rules. See Tu 2011, p. 687.

Issues Concerning Application of the Law of the People's Republic of China on Choice of Law for Foreign-Related Civil Relationships" ("SPC Interpretation 2013") does not contain any presumptory rules, this development calls for a number of questions. Where to search for presumptory rules in the absence of a valid source of law? Does this development signify a change in the Chinese rules of private international law, which have been earlier so strongly characterised by the pervasive application of presumptory conflict rules?

Most of the problems related to the research and interpretation of foreign law or, in a broader perspective, a legal system, relate to the fact that the subject matter of study is essentially foreign. Ascertaining the content of foreign law is and always will remain challenging, irrespective of whether it is the law of a geographically and culturally distant country or the law of a neighbouring country. In the case of Chinese law, a foreign researcher should always remember that the indigenous Chinese legal tradition, influenced by references to socialism, Confucianism and the transitional stage of the legal system, all remain to facilitate both the formation and interpretation of Chinese law.[46] Correspondingly, the interpretative remarks of this study have been attempted to be conducted with appropriate prudence.[47]

The author has chosen to continue to illustrate the Chinese choice-of-law rules premised on the presumptory rules featured in the SPC Interpretation 2007. This is a conscious choice. First of all, it is fairly hard to properly present the Chinese choice-of-law rules without a reference to the existence of presumptory rules so pervasively characterised in prior practice of Chinese private international law. Secondly, a fair amount of real arguments supports a perception that the SPC is about to introduce another judicial interpretation that is likely to more or less reinstate the conflict rules featured in the now-abolished SPC Interpretation 2007.[48] This observation functions as the justification to systematise the Chinese choice-of-law rules on a now-abolished source of law. On the other hand, such an approach also means that the interpretative remarks made concerning the application of the choice-of-law rules applied in CIETAC arbitration should count, for now, nothing more than an enlightened guess.

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[46] See Ruskola 2012, pp. 275 – 276; Peerenboom *et al.* 2010, pp. 38 – 39 and Jänterä–Jareborg 2004, pp. 193 – 194.
[47] In Clarke's view, Western lawyers who at first encounter Chinese law with a reaction anything else than perplexity are likely to have ineptly grasped the basics about China's legal system. Such remarks justify approaches that consider only a prudent and limited interpretation of Chinese law to be possible from a foreign perspective. See Clarke 2003, p. 93.
[48] See *infra* Chapter 4.2.3.

As the study features a comparison of two different sets of arbitration rules, it would seem self-explanatory that a method of comparative law is required. Because the contemporary ICC and CIETAC arbitrations operate in the same framework of international arbitration practice, national arbitration laws and, most importantly, the same clientele mostly comprehending of large and often multinational businesses, conventional wisdom has guided the author to use a functionalist approach as a method of comparison. Arguably the most renowned advocates of functionalism, Zweigert and Kötz, argue the basic methodological principle of all comparative law to be functionality. In their view, as the legal system of every society faces essentially the same problems, societies tend to solve these problems by quite different means though often with very similar results.[49] So when the comparatist attempts to compare, for instance, two different legal systems with each other and research how the same problem is resolved in these societies, the unconscious implication is to try to find the functional equivalents from the respective legal systems and search for the similarities and differences appearing in the two systems. As Örücü has aptly phrased it, the functionalist inquires how a certain legal problem encountered both in society A and B is resolved by their respective (legal or other) systems.[50]

Albeit functionalism remains to be the dominant paradigm of comparative law,[51] a critique of functionalist approaches has emerged in contemporary jurisprudence. Functionalist approaches, which identify criteria of comparison in terms not of rules but of problems, tasks, or societal needs met by law, are often held by cultural comparatists as deficient. According to Cotterrell, the deficiency of functionalism results from its failure to recognise the purposes and tasks of law are inevitably defined using the terms of reference provided by particular cultures.[52] For instance, the taxonomic project of law, i.e. the division to legal families embraced by Zweigert and Kötz, has devoted most of its work to laws originating from Europe, with the corresponding marginalisation of the other laws of the world.[53] Glenn argues that this results from the inherent Eurocentric bias of the legal family concept in favour of Western concepts of law and, in particular, the notion of the

[49] See Zweigert – Kötz 1998, p. 34.
[50] See Örücü 2004, p. 25.
[51] Platsas goes as far as to question whether a different kind of approach is even needed in comparative law studies. See Platsas 2008, p. 3.
[52] See Cotterrell 2006, pp. 710 – 711.
[53] While Zweigert and Kötz have the described the European legal systems in a total of 212 pages, the Islamic, Hindu, Chinese and Japanese legal systems have, in balance, only a description of 36 pages. In addition, Zweigert and Kötz dedicate the rest of their book to the notions of contract, unjustified enrichment and tort – which all three concepts are of European origin. See Zweigert and Kötz 1998.

legal system.[54] In the case of European legal systems, whereas Zweigert and Kötz consider one of the rationales for the use of functionalism to be the unification of law and demonstrate this, among other things, with the harmonisation work done in the European Union,[55] Legrand argues that simple legislative harmonisation on the surface level does not yet mean that the European legal systems would actually be converging.[56]

Teemu Ruskola has conducted his China-specific comparative research based on the functionalist critique. Whereas he does admit functionalism to be useful to a certain extent, he does conclude that it has a lot of limits. As *inter alia* Cotterrell, Glenn and Legrand have pointed out, these limits are typically related to the implicit functionalist assumptions about the problems that should be resolved by legal rather than some other means. In Ruskola's view, functionalism can in its worst lead to a kind of epistemological imperialism, in which we, i.e. Western lawyers, find in foreign legal cultures confirmation of the projected universality of our own legal categories, or, "proof" of the fact that other legal cultures lack some aspect or other of our law.[57] Ruskola concludes that the conception regarding the development of Chinese law is in essence a Western representation; as the legislative reforms concluded in China are based on Western ideas and methodology of law, they may, in the end, tell more about ourselves than they do of any equivalent (or even non-equivalent) phenomenon in China.[58] The post-1978 development of the Chinese legal system could have been, in Ruskola's words, 'self-Orientalisation' more than anything else.[59] Acknowledging this, Zhu Suli, a leading Chinese scholar, has suggested that modelling China solely by on the standards and interests of the West would be an unfavourable course of action.[60]

In light of the critique presented towards the functionalist method of comparative law, the author believes it would be too simplistic to dismiss the choice-of-law methodology applied in CIETAC arbitration as 'backwards'. Neither a dismissal of CIETAC arbitration as simply inadequate would provide any (new) knowledge regarding the possible advantages of using it as a method of Sino-foreign dispute resolution. Consequently, the author believes that it is much more fruitful to attempt

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[54] See Glenn 2006, pp. 434 – 435.
[55] See Zweigert – Kötz 1998, pp. 24 – 28.
[56] See Legrand 1996, pp. 54 – 64.
[57] See Ruskola 2002, pp. 189 – 191.
[58] Ibid, pp. 192 – 196.
[59] Ibid, pp. 197 – 199.
[60] See Peerenboom *et al.* 2010, p. 65.

to conduct the functionalist comparison in a self-conscious way, i.e. being aware of the inherent shortcomings and bias of the 'classical' functionalist method of comparative law.

Seppänen aptly notes that the applied research method and phrasing of research questions often determines the result of the study even before it has started.[61] Indeed, the functionalist comparison conducted in this study will, perhaps unsurprisingly, illustrate that whereas the ICC Rules leave a great deal of discretion regarding the arbitration procedure for the chosen arbitrators, the CIETAC Rules and Chinese arbitration law *de facto* impose heavy limitations on the arbitrators' discretion to decide upon the arbitration process.[62] As a result, the arbitrators' power to independently choose the law applicable to the merits of the dispute in the absence of the agreement of the parties is limited to exceptional circumstances.[63]

One could argue that the contemporary framework of international arbitral practice is apparently biased towards the preference of a delocalised or autonomous approach. The current embracement of the principle of party autonomy in international arbitration practice, for instance, is ultimately a result of the wishes and needs of the international business community.[64] In correspondence, the clientele-biased approach means that the established international arbitration practice, i.e. the terms of reference to evaluate the success or failure of arbitration rules, has been tailored to fit the needs of the international businesses – not the ones of, for instance, the Chinese Communist Party. This is not an argument in favour or against the emergence of a pro-autonomous regime of international arbitration. It simply reminds that the contemporary bias of international arbitration practice towards delocalised arbitration inevitably results in difficulties for (Western) legal scholars and practitioners to appreciate some of the solutions featured in Chinese arbitration.

In summary, the author believes that an analysis that would deem CIETAC arbitration as categorically lacking in comparison to ICC arbitration is an unsatisfactory one. The author would probably not have created any such knowledge that a prudent reader of this study would not already possess or at least have a clue about (which is, after all, the express objective of this study). Therefore, besides including a systematisation and contextual comparison of the subject matter of

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[61] See Seppänen 2005a, pp. 29 – 32.
[62] Perhaps an even more accurate way of phrasing this would be to assess that Chinese arbitration law does not confer CIETAC-administered arbitrations with the same powers as its counterparts in other national states. See *infra* Chapter 2.
[63] See *infra* Chapter 4.2.3.
[64] See Lew *et al.* 2003, p. 81.

study, the analysis will attempt to envisage such situations where the principle of party autonomy plays little or no role, or could be potentially remedied. By doing so, the research can also plausibly conclude that such situations do, at least in theory, exist where CIETAC arbitration may provide a rational alternative for ICC arbitration. As a result, an analysis of both added scientific and practical value is pursued.

1.4 Terminology

1.4.1 The meaning of 'international'

Generally speaking, the term 'international' is used to demarcate arbitrations that are purely national or domestic and those that in some way transcend national boundaries.[65] As some ambiguity exists regarding the interpretation of the term 'international' in the context of international commercial arbitration, a brief review regarding the possible semantic meanings of the notion is appropriate.[66] Firstly, the French method of classifying a dispute as 'international' relates to the character of the disputed transaction, i.e. if the underlying transaction has a foreign element, for example involves the import or export of certain goods, the dispute may be classified as international even in the event of both parties to the transaction are French citizens.[67] Other jurisdictions may, however, consider arbitration not be international if the parties to the dispute are both domiciled or habitually resident in that country, irrespective of the fact that there might be other contacts with foreign countries.[68] Finally, some jurisdictions may combine the subjective and objective criteria referred to and thus consider arbitration as international if either one of the parties resides or is domiciled abroad, or if the disputed transaction has an international character in that it is to be performed, to a significant extent, abroad.[69] Because different jurisdictions may have their

[65] See Redfern – Hunter 2009, p. 7.
[66] As the concept of international commercial arbitration generally refers to an out-of court resolution of disputes regarding transactions containing elements from two or more countries, Cordero-Moss points out that the semantic meaning of the word "international" has more to do in relation to the dispute than the arbitral process itself. See Cordero-Moss 1999, p. 43.
[67] See NCPC Art. 1492.
[68] See, for example, Swiss PILA Art. 176(1).
[69] The UNCITRAL Model Law takes this approach and further adds that arbitration may be qualified as international simply on the basis of the parties' explicit authorisation. See ML Art. 1(3).

own tests for determining whether an arbitration award is 'domestic' or, in the language of the New York Convention, 'foreign', this ambiguity may cause problems.[70]

Chinese arbitration law adopts a unique method to determine whether a dispute is considered international or not. China's law on arbitration has traditionally adopted a dual regime for foreign-related and domestic arbitration, with foreign-related arbitration institutions exercising jurisdiction over disputes involving foreign-related elements and domestic arbitration dealing exclusively with disputes arising between Chinese entities.[71]

Albeit the jurisdiction of foreign-related arbitration institutions, such as the CIETAC, has been later extended to cover also domestic disputes and vice versa, the Chinese classification of disputes (and consequently, the nationality of the rendered awards) to 'foreign', 'foreign-related' and 'domestic' remains.[72] According to a recent interpretation issued by the Supreme People's Court, a dispute may be classified as foreign-related if:

> (1) either party or both parties are foreign citizens, foreign legal persons or other foreign organisations, or stateless persons;
>
> (2) the habitual residence of either party or both parties is located outside the territory of the People's Republic of China;
>
> (3) the subject matter is outside the territory of the People's Republic of China;
>
> (4) legal facts that establish, alter or terminate the civil relation occurred outside the territory of the People's Republic of China exist; or

[70] According to Art. I(1) of the New York Convention, 'foreign awards' are defined as awards which are made in the territory of a State other than the State in which recognition and enforcement is sought; but it adds to this definition, awards that are 'not considered as domestic awards' by the enforcement State. In consequence, an award that one State considers to be 'domestic' (because it involves parties who are nationals of that State) might well be considered by the enforcement State as not being domestic (because it involves the interests of international trade). See Redfern – Hunter 2009, pp. 10 – 11.

[71] See CAL Chapters II and VII respectively regarding the distinct requirements set for both domestic and foreign arbitration commissions.

[72] See Gu 2013, pp. 91 – 92 and Chi 2009, pp. 545 – 546.

(5) other circumstances that may be determined as foreign-related civil relations exist.[73]

The classification of the dispute as either international or domestic has under Chinese law, *inter alia*, a direct effect on the scope of the parties' autonomy and the enforcement of the rendered award. For instance, the parties are allowed to choose a foreign law as the substantive law only in foreign-related arbitration.[74] In addition, the dual-track policy favours foreign-related arbitration in comparison to arbitration procedures involving domestic parties as it subjects domestic awards to both substantial and procedural review in the enforcement stage.[75] Based on the New York Convention, Chinese courts may subject only the procedural aspects of foreign-related awards for review.[76] On the other hand, both the procedural and substantive issues of domestic awards may be reviewed again by Chinese courts.[77]

Chi and Gu have suggested that the Chinese approach both seriously harms the efficiency of arbitration and meaninglessly wastes limited judicial resources of the Chinese courts, as the substantial review of domestic arbitral awards constitutes a *de facto* appeal or retrial of the case.[78] As a result of the discriminatory Chinese arbitration regime towards domestic parties, there have been instances in which purely Chinese parties have attempted to artificially include foreign elements in their agreements in order to avoid the application of mandatory provisions or regulations of Chinese law or, alternatively, to choose the place of arbitration overseas.[79] Nonetheless, the content of the most recent SPC judicial interpretation regarding Chinese rules of private international law would not seem to indicate any changes to existing practice, which forbids such measures.[80] Correspondingly, the Chinese method of classifying of disputes should be, for the purposes of this study, thoroughly understood.

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[73] See Art. 1 of the SPC Interpretation 2013.
[74] See CCL Art. 145.
[75] See Chi 2009, pp. 545 – 547. Chi suggests that foreign-related awards are deemed "quasi-Convention-awards" under Chinese arbitration law. Ibid. Concerns related to the weaker expertise of Chinese local arbitration commissions have been suggested to be the rationale of the dual-track system. See Gu 2013, p. 87.
[76] See CPL Art. 269 and New York Convention, Art. V and Gu 2013, pp. 116 – 117.
[77] See CPL Art. 217(2) and (3).
[78] See Chi 2011, pp. 280 – 281; Chi 2009, pp. 553 – 554; Gu 2013, pp. 130 – 131 and Gu 2008, p. 133.
[79] See Chi 2009, p. 547.
[80] According to Article 11 of the SPC Interpretation 2013, artificially created connecting factors that are meant to avoid the application of mandatory provisions of law or administrative regulations of the PRC, will not produce any validity regarding the application of any foreign law.

1.4.2 The meaning of 'commercial'

The term 'commercial' is generally understood as a reference to transactions carried out by business entities in the course of their daily business. None of the major arbitration treaties, such as the Geneva Protocol or New York Convention, attempted to formally define the notion 'commercial'. However, they did assume that 'commercial matters' could be arbitrated, while other matters may not. This was, however, was left to each Contracting State to regulate.[81] Even the drafters of the UNCITRAL Model Law left it to any Contracting State to decide for themselves what is meant by 'commercial'.[82] The only guidance of international origin regarding the interpretation of the notion may be found from the *travaux preparatoires* of the Model Law.[83] According to them, the notion 'commercial' should be given a wide interpretation so it would cover matters arising from all relationships of a commercial nature, whether contractual or not.[84] While the referred footnote does also include a non-exhaustive list of transactions that are to be considered of a commercial nature, it seems advisable to rather exclude certain areas of law that certainly do not fall within this category than to attempt to make a positive definition of what is commercial.[85]

[81] The text of the New York Convention allows for Contracting States to declare that it will only apply the Convention to matters considered commercial under its national legislation. This clause is referred to as the commercial reservation. See New York Convention, Art. I (3) and Redfern – Hunter 2009, pp. 12 – 13.
[82] Ibid.
[83] At least to a certain extent, national courts have been explicitly authorised to use the preworks of the Model Law as a source of interpretation. See Holtzmann – Neuhaus 1989. Some common law countries, however, have been noted to disallow references to *travaux preparatoires* of the ML. See Craig – Park – Paulsson, p. 520, fn. 4.
[84] See UNCITRAL ML, Article 1(1), fn. 2.
[85] See Cordero-Moss 1999, p. 45.

2 The Choice-of-Law Methodology Applied in International Arbitration

2.1 Jurisdictional and Delocalisational Theory

The choice-of-law methodology applied in international arbitration has undergone through major development during the past few decades. Today, the more 'modern' international arbitration institutions perceive arbitration as a completely independent and anational method of dispute resolution functioning outside the jurisdiction of national courts and legislation. In order to maximise party autonomy and procedural flexibility, contemporary arbitration scholars have stressed one of the key factors regarding to the acceptability of a contemporary procedure of international arbitration to be whether the arbitration respects the principle of party autonomy in an adequate manner. In order to achieve this objective, contemporary theory of international arbitration has correspondingly 'delocalised', meaning that the parties and their chosen arbitral tribunal are, at least in theory, allowed to exercise full control over the determination of the substantive law.[86]

Disputes submitted to international arbitration were once, however, perceived to be on the same level as domestic ones. Such a point of view, often referred to as the jurisdictional theory of international arbitration, was common in the first half of the nineteenth century and still affirmed in the Resolution of 1957 made by the XIVth Commission of the Institute of International Law, named "Arbitration in Private International Law".[87] Also known as the traditional approach of private international law, the jurisdictional theory refers to the full correspondence between the law of the arbitral venue and the law governing the arbitral proceedings.[88]

Under the approach embraced under the traditional doctrine, the arbitral tribunal applies the private international law of the *lex loci arbitri* to identify both the law governing the capacity of the parties to arbitrate and the substantive law governing the merits of the dispute.[89] In addition, the arbitral tribunal also applies the *lex loci arbitri* to the procedural aspects of arbitration[90] and to the validity of the arbitration clause.[91] Traditional methodology is typically applied by national courts, which

[86] See Born 2009, pp. 81 – 83; Saarikivi 2008, p. 57; and Fouchard – Gaillard – Goldman 1999, pp. 785 – 786.
[87] See Várady – Barceló – von Mehren 1999, p. 618 and IIL Yearbook 1957, pp. 491 – 496.
[88] See Born 2009, pp. 2119 – 2121 and Cordero-Moss 1999, p. 182.
[89] See Articles 4 and 11 of the Resolution of 1957.
[90] Ibid, Articles 8, 9, 10 and 12.
[91] Ibid, Articles 5 and 6.

are bound to apply the choice-of-law rules provided by the law of the state in which the court is situated (*lex fori*).[92]

Most arbitration scholars, however, consider the application of the jurisdictional theory in proceedings of international arbitration as inadequate and outdated.[93] Much of the attraction of the traditional approach has relied upon its ability to provide the arbitrator with a *lex fori*. Contrary to litigation, arbitral tribunals do not, however, have a *lex fori* in the same sense as national courts do.[94] This observation has also functioned as the main argument for the gradual abandonment of the jurisdictional theory regarding disputes submitted to international arbitration.[95]

The efforts to delocalise arbitration have, however, met resistance from national states that have proven to be reluctant to waive their judicial jurisdiction in favour of private justice. As a result of this reluctance, even the most widely accepted and celebrated transnational instruments governing contemporary international commercial arbitration, such as the New York Convention, are compromise solutions rather than perfect legal documents.[96] Indeed, the more progressive instruments concerning international arbitration have been noted to be rather regional than worldwide efforts to date.[97]

With regard to private international law, the introduction of the European Convention was the first step towards delocalisation. Signed in Geneva on 21st of April 1961 and aimed at promoting trade between the Cold War blocs, the European Convention was first regional convention to feature independent choice-of-law rules for arbitration.[98] Although the practical significance of the European Convention has been noted to be far from that of, for instance, the New York Convention, the referred Article VII had a considerable impact upon later arbitration rules and texts.[99]

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[92] See Lew *et al.* 2003, pp. 73 – 74 and Saarikivi 2008, p. 43.
[93] See IIL Yearbook 1989, p. 194; Fouchard – Gaillard – Goldman 1999, pp. 866 – 867 and Wortmann 1998, pp. 105 – 107.
[94] In the words of Lew *et al.*: "Since international arbitrators owe a duty to the parties rather than the sovereign, they need not to implement or follow state policies." See Lew *et al.* 2003, p. 426 and also Liukkunen 2013, p. 204.
[95] See Lew *et al.* 2003, p. 415 and Fouchard – Gaillard – Goldman 1999, pp. 637 – 638.
[96] The often-cited words of Judge Stephen Schwebel aptly describe the New York Convention: "It works." See Born 2009, p. 94 and Craig – Park – Paulsson 2000, p. 680.
[97] See Lew *et al.* 2003, pp. 19 – 21.
[98] See Art. VII of the European Convention.
[99] See Lew *et al.* 2003, pp. 21 – 22 and Fouchard – Gaillard – Goldman 1999, pp. 137 – 142. The independent choice-of-law rule of European Convention has been remarked to inspire the UNCITRAL Rules of 1976 and the ICC Rules of 1975. See Art. 33(1) of the UNCITRAL Rules 1976; Art. 13(3)-(5) of ICC Rules 1975 and Lando 1991, pp. 130 – 132.

The turning point regarding the acceptance of the delocalisational theory in international arbitration has arguably been the work of the XVIIIth Commission of the Institute of International Law, which officially questioned the appropriateness of the application of the jurisdictional theory in international arbitration. After a lengthy consideration, the XVIIIth Commission decided in its Final Report to deny the subjectivity of international arbitration to any national law and thus affirmed the detachment of arbitration from national law.[100] In fact, the General Reporter even opined that the only source of the arbitrators' jurisdiction should be the will of the parties even in situations when the parties' expressions would be contrary to the mandatory rules of a national law closely connected with the arbitral process.[101]

This being said, the delocalisational theory met strong criticism from several scholars who participated in the preparation of the Resolution of 1989. For instance, a member of the XVIIIth Commission succinctly remarked that "arbitrations do not take place in a vacuum but instead, they do take place in territories of national states", which may limit the parties' autonomy by the means of restrictive law on arbitration.[102] Arguably in consequence of the appropriate critique, the Final Draft of the Resolution of 1989 was approved with a vote of only a slight majority.[103] The debate between the supporters of the jurisdictional and delocalisational theory has continued ever since, and has been described to have arisen even to "religious" proportions.[104]

In correspondence with the acceptance of the delocalised approach advocated in the Resolution of 1989, more 'modern' choice-of-law rules, such as the direct method, have emerged and gradually gained acceptance in the arbitration rules of the major international arbitration institutes[105] and, to a

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[100] According to von Mehren, "the arbitral process is autonomous except in two situations: (1) where the process seeks assistance from the courts; and (2) where the process is conducted in a manner that disturbs the peace or deeply offends local values and morals. Neither of these situations is of sufficient importance or frequency to falsify the generalisation that, for all practical purposes, today arbitration, at least as so far as procedure is concerned, can be autonomous or anational". See Preliminary Report by A. von Mehren; and also Draft Final Report and the Final Report, which both confirm the Commission's pro-autonomous attitude regarding international arbitration practice. See IIL Yearbook 1989, pp. 44, 107 and 194 and also Cordero-Moss 1999, p. 181.

[101] See IIL Yearbook 1989, p. 140.

[102] Such a concern was originally expressed by F.A. Mann, a renowned English solicitor. See IIL Yearbook 1989, p. 173 and also Lew *et al.* 2003, p. 66.

[103] See Cordero-Moss 1999, p. 183.

[104] Ibid, p. 185.

[105] See Art. 35(1) of the UNCITRAL Rules 2010; Art. 28(1) of the AAA/ICDR Rules; Art. 22(3) of the LCIA Rules and Art. 22(1) of the SCC Rules.

lesser extent, national arbitration statutes.[106] In the context of contemporary international arbitration, the approaches used to determine the law applicable to the merits of the dispute are thus today commonly referred to as the indirect method (*voie indirecte*) and the direct method (*voie directe*).[107] On the one hand, the indirect method directs the arbitral tribunal to use a conflict of laws analysis to determine the applicable law, for instance, by imposing upon the arbitral tribunal the duty to apply the conflict of laws rules that it deems applicable or appropriate. On the other hand, the direct method guides the arbitral tribunal to directly apply the law it deems appropriate without the need to refer to any conflict rules.[108] In comparison to approaches requiring a conflict of laws analysis, the benefits of the direct approach are seemingly obvious: it allows for the arbitral tribunal to focus on the determination of the most appropriate law instead of having to focus on an often-complicated choice-of-law analysis.[109] Indeed, the success of the *voie directe* has been argued to be connected with the endavours to develop a transnational commercial legal order with arbitration as its supranational method of dispute resolution.[110] Some of the more radical ideas envisioned under the delocalisational theory, such as the idea about a universal *lex arbitri*, remain to be an oxymoron.[111]

Although time has taken its toll regarding the acceptance of the jurisdictional theory amongst international arbitration scholars, the apt critique presented towards the delocalised approach remains to be of practical value to date. Albeit the bulk of all arbitrations are today conducted without any reference to the law that governs the proceedings, it does not mean that the *lex arbitri* would not exist. Indeed, arbitration rules are only binding by virtue of the intentions of the parties; the restatement of the principle of autonomy in the arbitration rules amounts to no more than an affirmation by the parties themselves of their own autonomy. In the end, it is only national law that

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[106] See, for instance, Art. 1496(1) of the NCPC. On the other hand, most national choice-of-law statutes do, however, still require the authority applying the law to use a conflicts of law analysis to determine the substantive law. See, for instance, Rome I Art. 4(1) and, for the purposes of this study, Art. 41 of the Chinese LAL.
[107] See Ferrari – Kröll *et al.* 2010, pp. 264 – 265.
[108] The arbitrators' broad discretion under the *voie directe* does not disclose the possibility for the arbitral tribunal to resort to a conflict of law analysis. See Fouchard – Gaillard – Goldman 1999, p. 869. As Ferrari – Kröll *et al.* point out, the direct approach owes a lot to choice-of-law rules; in practice, the application of the *voie directe* may actually hide a conflict of law analysis. See Ferrari – Kröll *et al.* 2010, pp. 304 – 305.
[109] See Ferrari – Kröll *et al.* 2010, p. 294. On the other hand, Gaillard has assessed that the UNCITRAL method, closest connection doctrine and *voie directe* are all "three paths leading to the same result". See Gaillard 2004, p. 205. In the author's opinion, the comparison conducted *infra* in Chapter 4.3 is a fine illustration regarding the possible discrepancies of the indirect and direct method when put to practice.
[110] See Saarikivi 2008, p. 67.
[111] See Redfern – Hunter 2009, p. 89.

can provide the basis for party autonomy and determine the conditions and limits within which it can be exercised. That law will be either that of the *lex arbitri* or the laws of all the jurisdictions willing to recognise an award that has given effect to the parties' choice of applicable law.[112] With regard to national legislators which have implemented the Model Law (or a similar arbitration statute), it is the established interpretation of Article 28 of the ML, which ultimately unties the arbitrators from the choice-of-law rules of the *forum* country unless otherwise agreed by the parties.[113]

It would not be false to state that both of the described methods of reasoning regarding the determination of the applicable law, i.e. choice-of-law methodology based on the jurisdictional and delocalisational theory, continue to enjoy the support of international arbitration practice – at least to a certain extent. It would also be true to state that the application of both the choice-of-law methodologies can *per se* lead to a fair result. As a preference for an autonomous procedure of international arbitration has emerged, a choice-of-law methodology, which stresses the importance of the parties' and their chosen arbitrators' discretion and the actual result achieved in the determination of the substantive law, would indisputably seem to reflect the desired state of affairs much better.[114]

2.2 Different Choice-of-Law Methodology – Different Agenda?

As illustrated *infra* in Chapter 4, ICC and CIETAC arbitrations continue to apply different choice-of-law methodology to date despite they both operate in the same context of contemporary international commercial arbitration. Should the CIETAC modernise its choice-of-law rules, it is plausible that foreign parties would perceive it as a more favourable venue for proceedings of international arbitration.[115] Therefore, the question arises: why has the choice-of-law methodology applied in CIETAC arbitration not been revised, although it admittedly tries to make its arbitration to match international standards? Perhaps the most intuitive starting point for most people would be to guess that whereas the ICC is a non-governmental organisation that has always been advocating

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[112] See Lew *et al.* 2003, p. 667 and Fouchard – Gaillard – Goldman 1999, pp. 784 – 786.
[113] See Lando 1991, p. 131. Article 28(2) of the Model Law, or the "UNCITRAL method", has been considered the point of departure for all countries willing to modernise their national arbitration legislation. See Saarikivi 2008, p. 60; Gaillard 2004, p. 202 and *supra* Chapter 1.1. Saarikivi notes that even such national legislators, which have enacted "arbitration-friendly" legislation, retain the power to withdraw such law on arbitration. See Saarikivi 2008, p. 85.
[114] See Gaillard 2004, p. 192; Fouchard – Gaillard – Goldman 1999, p. 865; and IIL Yearbook 1989, p. 637.
[115] See *infra* Chapter 3.2.2.

for the promotion of international trade and investment, the CIETAC operates under the auspices of the People's Republic of China, a single-party authoritarian state based on socialist ideology. In other words, the likely explanation for the existing discrepancies of two institutions would be very different historical and socio-political background. However, accusing the CIETAC for many of its current defects would be barking up the wrong tree.

To begin with, the International Chamber of Commerce was founded in 1919 by businessmen from various countries that had been involved in the First World War. Its establishment was based on the idea that increasing trade between nations would contribute to world peace.[116] Contrary to at least the most if not all other arbitration institutes, the ICC International Court of Arbitration, located in Paris, France, does not itself settle disputes but instead functions as an administrative body. In this capacity, it *inter alia* supervises the arbitrations' compliance to the ICC Rules during the proceedings.[117] The arbitrations conducted via the ICC operate through its representatives from all over the world.[118] Because of its unique structure, the ICC has been noted to have the least national character compared to any of the other leading arbitral institutions.[119]

The ICC represents the voice of the international business community.[120] Throughout its existence, the ICC has actively contributed to the development of the conventions[121] applied in contemporary international arbitration – albeit with mixed success.[122] In correspondence with its agenda on delocalisation,[123] the ICC was amongst the first arbitration institutions to implement solutions that reflect the delocalised approach in its arbitration rules. For instance, the exclusion of a reference to a *lex fori* was confirmed the 1975 revision of the ICC's arbitration rules.[124] As to the determination

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[116] See Preamble and Art. 2 of the ICC Constitution.
[117] See http://iccwbo.org/About-ICC/Organization/Dispute-Resolution-Services/ICC-International-Court-of-Arbitration/Functions-of-the-ICC-International-Court-of-Arbitration/. Last visited 12th of December 2013.
[118] The national committees of the ICC currently comprise of more than 100 members from about 90 countries. See http://iccwbo.org/about-icc/organization/dispute-resolution-services/icc-international-court-of-arbitration/ for an up-to-date list of the current court members. Last visited 17th of December 2013.
[119] See Born 2009, p. 153.
[120] See Lew *et al.* 2003, p. 18.
[121] The Geneva Protocol, Geneva Convention and New York Convention all are directly based on the initiatives made by the ICC. Ibid, pp. 20 – 21.
[122] The final text of the New York Convention did not accept the ICC's more radical proposal, which would have extended its scope of application to 'international arbitration awards' instead of 'foreign arbitral awards'. See Craig – Park – Paulsson 2000, p. 680 and Cordero-Moss 1999, p. 187.
[123] See Craig – Park – Paulsson 2000, p. 8.
[124] See ICC Rules 1975, Art. 11. The substance of this Article has not been amended ever since. See Craig – Park – Paulsson 2000, p. 323 and Cordero-Moss 1999, p. 212.

of the substantive law, the direct approach was first featured in the 1998 revision of the ICC Rules.[125]

On the other hand, the foundation of the CIETAC[126] dates back to China's 'short golden period' of legislative development of the 1950s.[127] It was originally founded by the China Council for the Promotion of International Trade ("CCPIT") in 1956 to facilitate trade, in particular, between China and the Soviet Union.[128] However, the 'arbitration' conducted in the predecessors of the CIETAC was not arbitration in the sense as understood with the contemporary notion of international arbitration. For instance, the (domestic) arbitral awards rendered were not binding upon the parties, and the arbitral procedure was severely lacking in terms of judicial independence and party autonomy.[129] In practice, there was little use for foreign-related Chinese arbitration before the end of the Cold War.[130]

In correspondence with a market economy's needs to have means for the protection of property rights, the impetus for the development of foreign-related arbitration in China is rigidly related to the adoption of the policy of opening up and economic reform.[131] From 1988 onwards, the legal status of the CCPIT was amended from a government institution to a non-governmental organisation. In addition, the CCPIT began to simultaneously use the name China Chamber of International Commerce ("CCOIC").[132] This marks the beginning of China's arbitration reforms towards international standards. China's accession to the New York Convention in 1987[133] and the

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[125] See ICC Rules 1998, Art. 17(1).
[126] The CIETAC was formerly known as the Foreign Trade Arbitration Commission ("FTAC") and the Foreign Economic and Trade Arbitration Commission ("FETAC"). Despite the several name changes, the FTAC, FETAC and CIETAC always have been regarded as the one and same arbitral institution. See Tao 2012a, p. 21.
[127] See Luo 2005, pp. 3.
[128] The CCPIT was the national state body charged with the promotion of international trade in the People's Republic of China. See Tao 2012a, pp. 7 – 8.
[129] See Tao 2012a, pp. 1 – 3.
[130] Although China and the Soviet Union did have economic cooperation during the 1950s, the deteriorating relationship between the two countries brought them to a brink of war during the Cultural Revolution. China remained completely boycotted by Western countries until the 1980s. Peerenboom notes that the amount of foreign investment in China remained low before the introduction of the 'socialist market economy' in 1992. See Tao 2012a, pp. 23 – 24; Paltamaa – Vuori 2012, pp. 66 – 69 and 207 – 209 and Peerenboom 2002, p. 463.
[131] See Lubman 1999, p. 174 and Peerenboom – He 2009, pp. 9 – 10.
[132] See Tao 2012a, p. 22 and CCOIC Official Website: http://www.ccoic.cn/. Last visited 7th of January 2014.
[133] See the Decision on China joining the Convention on the Recognition on and Enforcement of Foreign Arbitral Awards, adopted by the National People's Congress Standing Committee on 2 December 1986 and effective from 22 April 1987.

adoption of the first version of the Chinese Arbitration Law in 1994[134] have been considered important steps in this development. As a result, the popularity of the CIETAC as a forum for settling international commercial disputes has risen correspondingly.[135] Since its inception, the CIETAC's arbitration rules have been amended seven times in total,[136] the latest revision being the one elaborated in this study.[137]

The CCOIC generally functions as a chamber of commerce in the same way as its counterparts overseas. Formally, it is charged with the responsibility for the organisation and establishment of foreign-related arbitration commissions (i.e. CIETAC and CMAC) in accordance with the Chinese Arbitration Law, and the formulation of arbitration rules for China's foreign-related arbitration commissions.[138] According to Tao, an admittedly close relationship between CCOIC and CIETAC does exist. In his opinion, it would be incorrect to claim that the CIETAC is controlled by CCOIC. Instead, the CIETAC functions independently in handling arbitration disputes and is free from the interference of any organisation or individual – as required by Article 8 of the CAL.[139]

The contemporary agendas of the ICC and CCOIC thus appear to resemble with each other. As China remains to be a single-party authoritarian state, any comments that emphasise the independence of Chinese arbitral institutions probably have a dubious sound for a Westerner.[140] To sum up, may CIETAC arbitration be trusted insofar as it can provide a fair and effective means of international commercial dispute resolution? Although CIETAC-administered arbitrators admittedly have some issues with transparency and the choice of arbitrators, it does not mean that it would not offer satisfactory arbitration services. In the author's opinion, the CIETAC should not be blamed for, *inter alia*, the low choice-of-law power of CIETAC arbitral tribunals.[141]

In fact, the absence of independent choice-of-rules in CIETAC arbitration is ultimately due to the restrictive Chinese *lex arbitri*. This is because CIETAC arbitration centres are, with the exception of the new Hong Kong venue, located in mainland China. As a result, the *lex arbitri* of CIETAC

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[134] See Arbitration Law of the People's Republic of China, as promulgated by Decree No.31 on 31st of October 1994.
[135] See Gu 2013, p. 78.
[136] See Tao 2012a, p. 23 and Zesch 2012, p. 284.
[137] Rules of Arbitration of the China International Economic and Trade Arbitration Commission, as amended and effective from 1st of May 2012.
[138] See Tao 2012a, pp. 22 – 23.
[139] Ibid.
[140] See *infra* Chapter 3.1.1 regarding Western Orientalism.
[141] See *infra* Chapter 3.2.2 regarding the CIETAC's reputation and proceedings.

arbitrations will, in practice, be the law of the PRC.[142] Now, while the UNCITRAL Model Law has influenced the CAL, the CCP has decided not to implement the Model Law nor modernise the Chinese Arbitration Law after its inception.[143] Moreover, neither the CAL nor the Chinese Civil Procedure Law offer any unequivocal guidance for CIETAC arbitrators regarding the determination of the substantive law.[144]

Again, it has been traditionally understood that whenever national arbitration law does not confer the arbitral tribunal the power to apply the choice-of-law rules it deems applicable, the choice-of-law rules of the seat country are to be applied. Therefore, the fact that the Chinese Party-state has not revised its national arbitration law – regardless of what the CIETAC or CCOIC wish for – is the ultimate reason to the current default application of the Chinese choice-of-law rules in CIETAC arbitration. In other words, the CIETAC Rules may not provide separate choice-of-law rules for arbitration before Chinese arbitration law allows for this.[145]

Prior to the acceptance of the delocalisational theory, the application of the choice-of-law rules of the forum country in international arbitration was not unique at all. Several countries, such as the United Kingdom, have not traditionally had separate choice-of-law rules for arbitration.[146] Today, the traditional approach is applied only in countries in where arbitration institutions retain a close connection with the state.[147] Indeed, the analysis of this study indicates that China is a prime example of such a country.

Although vowing to continue its economic and legal reforms, the Chinese Communist Party is arguably reluctant to make any comprehensive reforms to the Chinese arbitration regime. Should the Chinese government be truly committed to ensure that the CIETAC is an effective and satisfactory means for the resolution of international commercial disputes in comparison to the other arbitral institutions, it would make sense for the CCP to allow for the modernisation of the CAL. Subsequently, a full-range reformation of the Chinese arbitration law could function to

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[142] See *infra* Chapter 4.2.1 regarding the rigid applicability of the CAL in CIETAC arbitrations. As Hong Kong SAR is a separate jurisdiction from mainland China, the recently opened CIETAC venue in Hong Kong SAR might prove to be an exception to this rule of thumb. However, a thorough analysis of this topic may not be provided in this study.
[143] See Moser *et al.* 2007, pp. 47 – 48.
[144] See *infra* Chapter 4.2.3.
[145] See Lando 1991, pp. 132 and 137 – 138
[146] Ibid.
[147] See Lew *et al.* 2003, pp. 75 – 76.

improve the reputation of the CIETAC from a foreigners' perspective. Due to the said contradiction, a thorough discussion regarding China's transition to a country ruled by law and its implications to CIETAC arbitration would seem necessary before it may be appropriately compared to ICC arbitration.

3 China's Transition and the CIETAC

3.1 Historical Perspective

3.1.1 The Imperial, Republican and Maoist Era

Many still tend to question whether law has ever had anything to do with the Chinese society.[148] In fact, a thesis about China's lawlessness is not new at all. Western jurisprudence has questioned the very existence of law in China for hundreds of years, beginning from the works of Baron de Montesquieu, Karl Marx, Max Weber and Georg Wilhelm Hegel. Under these 'Orientalist' views, China has been considered a fictitious adversary of the European countries.[149] This perception is based on the observation that China has traditionally lacked a European-style comprehensive formal–rational system of law with the exception of criminal law codifications (*fǎ*).[150] Formal law in China has thus traditionally not been associated at all with what Western jurisprudence understands with the notion of private or civil law. Instead, the Chinese society has traditionally chosen to rather control private property and contractual relationships by the rule of morality and virtue (*lí*), a notion typically associated with Confucianism.[151]

After the humiliating loss of the Chinese Empire in the Opium War to the Western colonial powers led by Great Britain, the Qing Dynasty decided to reform of its governing system based on Western models. By 1911, the first comprehensive Chinese civil codifications modelled on Japanese, French and German civil codes had been introduced.[152] After the Chinese uprising, the new Republican government re-promulgated these codifications without significant changes and continued the legal reform based on the heritage of the Qing Dynasty.

The reforms of the Imperial and Republican era, however, never managed to gain a proper foothold in the Chinese society due to the shortage of legally educated people, various civil wars and the

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[148] Such a rough statement has been extended to concern (Western) laypersons, practitioners and even scholars. See Seppänen 2005a, p. 17 and Peerenboom 2002, pp. 1 and 559.
[149] See Chen 2008, pp. 8 – 9; Seppänen 2005b, pp. 588 – 589 and Ruskola 2002, pp. 213 – 215.
[150] The earliest Chinese legal codifications date back to as early as 500 BC, which are all solely concerned upon criminal law. See Chen 2008, pp. 9. The negative Chinese connotations associated with *fǎ,* i.e. "formal law", date back to the arbitrary rule of the first Chinese emperor, Qin Shi Huang. As the Chinese society is strongly based in tradition, the notion of *fǎ* is still often attached to either administrative or criminal law in the legal consciousness of the Chinese layman. See Glenn 2006, pp. 306 – 309.
[151] See Ruskola 2012, p. 265.
[152] See Luo 2005, p. 51.

Sino-Japanese War.[153] Nevertheless, these reforms have contributed the development of the post-totalitarian[154] Chinese legal system, as it absorbs elements from the statute-based civil law legal systems applied in Continental Europe.[155] In fact, the notion 'party-state', used by the CCP today, has been noted to be inheritance from the earlier regimes in power.[156]

After the end of the Second World War, China descended into a civil war between the Communists and the Republicans. The Chinese Soviet Republic, led by the Chinese Communist Party and the charismatic Mao Zedong, gradually emerged as the reigning authority in mainland China. Subsequently, the People's Republic of China was formally founded in 1st of October 1949.[157] At first, the Communist regime seemed to be committed to establish a socialist legal system based on the Soviet model during the period between 1954 and 1957.[158] This development was derailed by the Anti-Rightist Campaign and the Great Leap Forward of the late 1950s, which led to the persecution of Chinese intellectuals who expressed dissenting opinions from the views of the CCP and, in particular, Mao Zedong.[159] All further legislative development was abruptly brought to a halt after the beginning of the Culture Revolution in 1966, during which Mao and his followers smashed the existing Chinese legal institutions into complete submission. As the case was with Imperial China, the totalitarian Chinese Party-state considered laws nothing else but tools of the state and the ruler; there were no effective legal limits on state power.[160] This 'rule by man', contrary to a 'rule of law', unquestionably and rightly served to strengthen the existing Western prejudices about the insignificance of law in the Chinese society.[161]

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[153] Ibid, pp. 52 – 53.
[154] The division to 'totalitarian' and 'post-totalitarian' China refers to the pre-1978 extreme-leftist Party-state in contrary to the post-1978 Party-state, which has more or less lost its belief to the reformation of the Chinese society on the basis of Socialist ideology despite the continuous references to socialism. See Paltamaa – Vuori 2012, pp. 14 – 16.
[155] See Peerenboom 2002, p. 1 and Luo 2005, pp. 51 – 53.
[156] See Peerenboom *et al.* 2010, p. 54.
[157] See Paltemaa – Vuori 2012, pp. 16 – 21. The Central Committee issued an order that abolished the Republican laws in February 1949. See Luo 2005, p. 53.
[158] See Seppänen 2005a, p. 52 and Luo 2005, p. 54.
[159] Ibid. Most of China's jurists, lawyers and judges ended up being victims of Mao's campaigns. See Håkansson 1999, p. 19.
[160] See Peerenboom 2002, pp. 46 – 49 and Lubman 1999, pp. 88 – 89.
[161] The reference to a 'rule by man' refers to the Maoist preference of a "legal system" amenable to manipulation of power instead of a 'rule of law', which requires processes to limit the arbitrary use of power. See Luo 2005, pp. 3.

3.1.2 The Post-Totalitarian Era

After Mao's death in 1976, China started to depart from the extreme-leftist ideology and policies as the pragmatist and reformist elites of the CCP gradually defeated the followers of the Maoist line and were restored to power. The new policy of opening up and economic reform (*gaige kaifang*), advocated by Deng Xiaoping in particular, refers to the series of economic reforms carried out in the PRC after 1978. In its earliest stage, it involved the decollectivisation of agriculture, the opening up of the country to foreign investment, and permission for entrepreneurs to start privately owned businesses.[162]

Although this study cannot fully elaborate the historical development of the post-totalitarian era, the embracement of the policy of opening up and reform deserves a remark as it represents a turning point in China's socio-economic development. After 1978, China's leaders have continued to gradually transform the Chinese society from a central-planned economy to a 'socialist market economy', albeit not without setbacks.[163] These setbacks are primarily related to the internal power struggles of the Chinese Communist Party and series of civil unrest, most important (and tragic) being the Tian'anmen Incident of 1989.[164]

Indeed, China's economic development tops the CCP's agenda to date. Even recently, the representatives of the most important organ of China's state apparatus, the Central Committee of the CCP, vowed to further deepen the policy of economic reform and opening up in its Third Plenary Session of its 18th CCP Central Committee Meeting held in November 2013.[165]

The agenda of economic reform also served as the CCP's incentive to promote the restitution of a legal system.[166] To cut a long story short, the disastrous effects of Mao's campaigns ensured that China's legal system has essentially been built from a complete scratch.[167] Taking this starting point into account, the legal reform conducted in the People's Republic of China has undisputedly

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[162] See Paltemaa – Vuori 2012, pp. 255 – 284. Clarke divides the reforms into four different stages, of which the latter stage is still currently a work in progress. See Clarke *et al.* 2006, pp. 11 – 14.
[163] The notion of 'socialist market economy' was introduced in 1992 in the 14th CCP Central Committee Meeting by the initiative of Jiang Zemin. The acceptance of this notion basically justified the dismantlement of the remnants of China's centrally planned economy. See Paltemaa – Vuori 2012, p. 340.
[164] Ibid, pp. 320 – 328; Peerenboom – He 2009, p. 4 and Peerenboom 2002, p. 58.
[165] See http://news.xinhuanet.com/english/china/2013-11/15/c_132891949.htm. Last visited 2nd of January 2014. On the *de facto* authoritative role of the Central Committee in the Chinese state apparatus, see Luo 2005, pp. 47 – 49 and Seppänen 2005a, pp. 55 – 56.
[166] See Lubman 1999, p. 102.
[167] See Lubman 2006, p. 6 and Peerenboom 2007, p. 20.

produced a remarkable outpouring of legislation and administrative rules in a relatively short period of time.[168] The development of the PRC Constitution of 1982, amended three times to date, reflects the gradual transformation of the Chinese society from a centrally planned economy toward a more market-oriented economy.[169] Contrary to the earlier PRC constitutions, the Constitutions' latest amendment now also endorses the basic principles of a government of laws, the supremacy of the law, and the equality of all before the law.[170] An abundance of new laws and various types of regulations has been enacted, legal institutions and education has been re-established, and the legal consciousness of the common layman has been improved.[171] This being said, as a result of the conflicting provisions of the Chinese constitutions as well as actual political practice, rule of law in China has, however, been traditionally fulfilled in relation to only individual cases at best.[172] As this remains to be the case to date, China's legal system has been aptly described to be in a period of "transition".[173]

3.2 Rule of Law in Contemporary China

3.2.1 Is China's Legal Reform Trapped in Transition?

The CCP's incentive to build a legal system is arguably originally related to the Weberian-North thesis regarding the necessity of law for sustainable economic development.[174] In other words, China's ruling elite has probably not viewed the development of the Chinese legal system as an absolute value *per se* but rather as means to promote China's economic development – arguably in order to seal its own political legitimacy amongst Chinese citizens.[175]

Albeit the sincerity of the CCP's motives to develop a legal system may thus be questioned, Chinese commentators claim that viewing the CCP as a hindrance to the development of China's legal system is an overly simplistic and erroneous purview.[176] In fact, the pragmatic approach of the Chinese government towards its reforms – both economic and legal – has been praised for even by

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[168] See Lubman 1999, p. 173.
[169] See Peerenboom 2002, p. 88 and Clarke *et al.* 2006, p. 7.
[170] See Peerenboom 2002, p. 89. Peerenboom, however, admits that with regard to the values embodied by the PRC Constitution of 1982, a gap between 'law in books' and 'law in action' continues to exist. Ibid, p. 214.
[171] Ibid, pp. 6 – 7.
[172] See Peerenboom *et al.* 2010, p. 28.
[173] See Lubman 2006, pp. 41 – 43 and Peerenboom 2002, p. 6.
[174] See Clarke *et al.* 2006, p. 2 and 37. and Peerenboom 2002, pp. 450 – 454.
[175] See Peerenboom – He 2009, p. 9 and Lubman 1999, p. 174.
[176] See Peerenboom *et al.* 2010, pp. 52 and 68.

Nobel-prize winning economists. Indeed, the Chinese efforts to develop its own variant of socialist rule of law compatible with its current form of government and contingent circumstances might, in retrospect, prove to be a better alternative than the wholesale import of the liberal democratic form of rule of law found in Euro-America.[177]

The CCP's reforms remain subject to two sharply differing views presented by both its critics and supporters.[178] But what should be thought out of China's legal system – can it and the CIETAC be trusted? The close relationship between China's ruling elite, judicial system and Chinese arbitration institutes constitutes for a discussion regarding the effects of China's ongoing legal reform to Chinese arbitration. After all, it would be redundant to contemplate upon the scope of the discretion of the Chinese arbitrators to, for instance, make decisions regarding the substantive law, if the arbitration procedure itself is either partial or arbitrary.[179]

Generally speaking, it is evident that China is still far from a country that respects the rule of law as understood in the West. In fact, it may very well be that it under the leadership of the Chinese Communist Party, China will neither achieve nor want to achieve that.[180] After all, it has been argued that the CCP values its control over Chinese society more than it does legal reform.[181] Should the CCP decide to abstain from giving up its control over the Chinese judiciary, it is likely that China cannot, in the long run, realise her full economic and political potential.[182]

This being said, one should not deduce that China has made no progress towards a society governed by a rule of law. Professor Randall Peerenboom, one of the most prestigious researchers of Chinese law, has aptly noted that whenever Western commentators claim that China lacks rule of law, they mean that China lacks the "thick" Liberal Democratic form found primarily in modern Western states with a well-developed market economy.[183] Thick conceptions add to the formal aspects of a rule of law the elements of political morality, forms of government or conceptions of human

[177] See Peerenboom *et al.* 2010, p. 31 and Peerenboom 2007, p. 5.
[178] Lubman and Peerenboom, for example, disagree with regard to whether China even has a "legal system" in the first place. See Peerenboom 2002, pp. 563 – 568 and Lubman 1999, pp. 317 – 318. Clarke *et al.* assess that describing the forces keeping China together especially during the two decades of its reform as a "political, social and economic equilibrium" would be closer to the truth. See Clarke *et al.* 2006, p. 31.
[179] See Peerenboom *et al.* 2010, p. 10 and Peerenboom 2007, pp. 1 – 10.
[180] In Luo's opinion, should the CCP not abandon its position as the sole ruling party, China may never achieve a "true" rule of law. See Luo 2005, p. 55.
[181] See Lubman 2006, p. 6.
[182] See Peerenboom *et al.* 2010, p. 23.
[183] See Peerenboom 2002, p. 5.

rights.[184] In Peerenboom's view, China's reference to a 'socialist rule of law', endorsed by the CCP, is rather an attempt to follow a "thin" version of rule of law, utilising only the instrumental aspects of the thick theory. A thin version of rule of law thus imposes at minimum some meaningful restraints on state actors.[185] However, the CCP's purview regarding what kind of a variant of a thin rule of law should be embraced remains unclear, although it evidently rejects the Liberal Democratic one.[186]

China has achieved a lot as a result of the said reforms. Pursuant to the legal reform, the CCP exerts much less control upon Chinese citizens in comparison to the Maoist Party-state. Moreover, a consensus exists regarding the increased significance of law in China and its commercial players, in particular.[187] This being said, pervasive shortcomings to the proper application of even a thin version of rule of law in China continue to exist. The said shortcomings are systematic and institutional in nature, typically associated with the paternalistic tradition of the Chinese society, fragmentation of authority between the central and local governments, large differences in regional implementation of laws and corruption.[188] As Chapter 4.2.3 vividly illustrates, ambiguity exists also regarding the proper interpretation and normative force of Chinese law. In fact, the problems related to the lack of transparency in Chinese law and regulation-making and their inconsistent implementation are amongst the primary complaints of foreign investors instead of, for example, the enforcement of contractual rights.[189]

For the purposes of this study, the issues related to the poor enforcement of arbitral awards call for further elaboration. Generally speaking, foreign parties tend to opt for arbitration instead of Chinese courts as they perceive arbitration as a method to avoid the ambiguities or biases of China's legal system.[190] Another perceived advantage of arbitration in comparison to judgments rendered from national courts is the higher degree of enforcement of arbitral awards because of the limited review

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[184] Ibid, p. 3.
[185] Peerenboom divides the competing variants to a Statist Socialist, Communitarian and a Neoauthoritarian one. Ibid, pp. 3 – 4 and 65.
[186] The chairman of the National People's Congress, Wu Bangguo, has been quoted to remark in 2009 that China will "never" copy the model of the Western democracies. See Paltemaa – Vuori 2012, p. 435. See also Peerenboom 2002, pp. 516 – 518.
[187] Ibid, pp. 6 – 8; Peerenboom *et al.* 2010, pp. 30 and 67 – 68 and Clarke *et al.* 2006, pp. 6 – 7.
[188] See Peerenboom *et al.* 2010, p. 36 and Peerenboom 2002, pp. 9 – 12.
[189] See Peerenboom – He 2009, pp. 4 – 5.
[190] See Gu 2013, p. 79 and Peerenboom 2001, p. 68.

possibilities of a foreign arbitral award under New York Convention.[191] However, the enforcement of arbitral awards in China has been traditionally portrayed as difficult.[192]

In most cases, it can be assumed that losing party will voluntarily comply with the decision of the arbitral tribunal.[193] Should the Chinese party whom the enforcement is being sought against obstruct the enforcement of the arbitral award, the dispute is placed back in the hands of the Chinese judiciary. This is due to the PRC courts' responsibility to enforce their own judgments and arbitral awards as well.[194] Hence, even a clause stipulating on overseas arbitration cannot categorically guarantee that Chinese courts could be avoided in a dispute featuring Sino-foreign parties.[195] However, Chinese courts may only review the procedural aspects of foreign arbitral awards in line with international practice and Article V(2) of the New York Convention.[196]

The correct instance to seek for the enforcement of an arbitral award in China is the appropriate Intermediate People's Court where the defendant is located or has assets.[197] There are several factors affecting the quality of the Chinese judiciary, such as the level of the court, the region, the type of case, and the division within the court.[198] A look into China's twentieth-century history reveals that the Chinese judiciary has traditionally been subordinated either to the Emperor, the National People's Congress, or party officials.[199] In consequence, Chinese judges have perceived themselves rather as civil servants than independent professionals, and have often left the articulation of dissenting opinions and interpretations to legal scholars.[200] Political corruption or, in other words, undue interference from party officials, may not be only the only source of influence

[191] See Redfern – Hunter 2009, p. 587 and Lew *et al.* 2003, p. 663.
[192] See Peerenboom – He 2009, p. 14; Peerenboom 2002, p. 463 and Håkansson 1999, p. 193.
[193] See Redfern – Hunter 2009, p. 622.
[194] See Peerenboom 2002, p. 287.
[195] Other instances in which the arbitration parties may be forced to resort to the assistance of Chinese courts include the enforcement of interim measures and, contrary to international practice, the evaluation of the validity of the arbitration agreement. See Gu 2013, p. 87.
[196] This definition excludes the public policy and social public interest grounds in which China does not have a fixed definition. Ibid. According to Tao, Chinese courts have not, for the time being, refused the enforcement of foreign arbitral awards under the *ordre public* ground. See Tao 2012a, p. 218.
[197] See Peerenboom 2001, p. 8.
[198] See Peerenboom 2007, p. 199.
[199] See Peerenboom *et al.* 2010, p. 28.
[200] Ibid, p. 60.

on courts; individual parties, the media, civil society and others may also exert direct or indirect influence on the courts.[201]

Instead of political corruption, the non-enforcement of foreign arbitral awards is seemingly more often linked with local protectionism. Local protectionism refers to the close economic or other inter-personal linkages between the Chinese judiciary and the Chinese party involved. The existence of such connections, or "*guanxi*", has been deemed of particular importance in Asian countries such as China; knowing the "right people" is often perceived to help litigators or lawyers to make things go more smoothly.[202] *Guanxi* in itself should not, however, be mixed up with corrupt practices. *Guanxi* is generally perceived to be legal, while corruption is not; it more often involves longer-term relationships than corrupt ones, and "builds on trust" rather than on a "commodity" exchange between money and power.[203] Needless to say, the difference between duly and unduly influence is a blurred one, and as significant economic interests are often involved in commercial disputes, it should come as no surprise that parties may attempt to use their connections to influence judges.[204] What seems less discussed is that not only foreign investors have to go along with local corruption, but that they may engage in illegal conduct themselves as well.[205]

Generally speaking, judicial corruption seems to exist in all main Chinese court divisions where key functional judicial power exists.[206] While the more visible issues with judicial corruption and competence has been identified to exist in the basic level courts, the judges in the more developed eastern region and larger cities are perceived to be more qualified than the ones in the western or middle region and in small towns.[207]As China's economic reform has progressed, the significance of single companies for local governments has decreased. In correspondence, the incentive of local governments to engage in corrupt practices, such as local protectionism, has also arguably

[201] Ibid, p. 67.
[202] Ibid, p. 213 and Clarke *et al.* 2006, pp. 35 – 36. Peerenboom notes that the use of social connections as a means to an end has, in the absence of a working market economy, been a matter of economic, social and political reality. See Peerenboom 2002, pp. 402 – 403.
[203] See Lubman 2006, pp. 70 – 71.
[204] See Peerenboom 2002, p. 403 and Peerenboom 2001, p. 67.
[205] See Lubman 2006, p. 75.
[206] Ibid, p. 220.
[207] See Peerenboom 2007, p. 199.

decreased. On the other hand, the enforcement of arbitral awards is likely to remain more difficult in poorer and less judicially competent jurisdictions.[208]

The available data on the enforcement of arbitral awards has been mostly courtesy of PRC sources, which have arguably provided a more favourable (and incomplete) perception regarding the enforcement of arbitral awards in China in comparison to the data gathered by foreign legal scholars.[209] This being said, the more recent studies indicate that in urban areas the enforcement of arbitral awards has significantly improved, and that non-enforcement of arbitral awards in China is rather related to the insolvency or encumbrance of the defendants' assets instead of, for example, local protectionism.[210] In addition, the SPC has taken measures in order to curb inappropriate review of arbitral awards, such as the pre-reporting system, which makes it mandatory for lower level courts to obtain the approval of upper level courts, and ultimately the SPC, for any decision that would lead into the non-enforcement of a foreign arbitral award. As a result of the promising development, the lack of the Chinese judges' experience in handling arbitration cases has been argued to pose the largest contemporary threat for the enforcement of foreign arbitral awards instead of corruption.[211]

To conclude, it seems that the days of arbitrary rule are now a matter of the past in China.[212] Whether the CCP is genuinely serious about addressing the rest of the issues related to the institutional framework of China's legal system remains, however, unanswered to date.[213] Notwithstanding the Chinese rhetorics on its struggle against corruption and the promotion of rule of law, the CCP's anticorruption and rule of law policies have arguably not yet risen to the top of its agenda.[214] Despite its shortcomings, China's legal system has been perceived to play a significant role in Chinese dispute resolution, although its quantitative significance cannot be judged in

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[208] See Peerenboom – He 2009, p. 15.
[209] Whereas a survey conducted by the CIETAC's Arbitration Research Institute in 1997 stated that 77 per cent of CIETAC awards and 71 per cent of foreign arbitral awards are enforced, Professor Peerenboom's own survey assessed the enforcement rate of CIETAC and foreign arbitral awards respectively to be around 47 per cent and 52 per cent. See Peerenboom 2001, pp. 2 – 5.
[210] See Peerenboom – He 2009, pp. 14 – 15.
[211] See Gu 2013, pp. 83 and 122 – 124.
[212] See Chen 2008, p. 653.
[213] See Peerenboom *et al.* 2010, p. 31. Clarke *et al.* assesses that China's legal development has not played an important role with regard to its economic success. See Clarke *et al.* 2006, p. 51.
[214] See Peerenboom *et al.* 2010, p. 32.

comparative terms because of the lack of systematic data.[215] Because an increased amount of Chinese government officials, policy makers, judges, academics, and non-governmental organisations perceive the existence of a reliable legal system and a more independent judiciary as a positive factor, the CCP seems now to be committed to the realisation of a thin variant of a rule of law out of necessity, if not anything else.[216]

3.2.2 Can CIETAC Arbitration Be Trusted?

Before going into the details of CIETAC arbitration, a disclaimer is in order. Premised upon the longstanding Chinese tradition of a society governed by *li*, Chinese parties are perceived to prefer informal means of dispute resolution through negotiation or mediation instead of litigation. Owing to the tradition of harmonious settlement of disputes, Chinese arbitration commissions even today tend to feature a possibility for 'harmonious arbitration', which is a mixture of mediation and arbitration[217]. Albeit Chinese parties prefer arbitration in comparison to litigation in general, it has been suggested that foreign parties should consider any formal means of dispute resolution as a last resort in order to avoid to damaging their commercial relationships with their Chinese partners.[218]

Nonetheless, growing international trade with China has resulted in the CIETAC to emerge as the busiest arbitral institution in the world since 1993, handling currently about 1300 cases per year on average.[219] Contrary to the ICC, the CIETAC has never enjoyed the prestige to contribute to the development of international arbitration. Instead, the CIETAC has had to focus its resources in order to convince (foreign) parties that it can offer a viable alternative compared to the other more reputed arbitral institutions.[220] Despite the numerous figure of handled cases and the Chinese efforts to internationalise and liberalise its organs and rules, foreign corporations, counsels and scholars

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[215] See Clarke *et al.* 2006, pp. 43 – 44.
[216] Ibid, p. 28.
[217] See Gu 2013, pp. 94 – 96. Zimmerman notes that this characteristic tends to bog down CIETAC-administered arbitrations. See Zimmerman 2010, p. 23.
[218] See Zesch 2012, p. 285; Seppänen 2005a, pp. 78 – 83 and Håkansson 1999, pp. 18 – 19. A World Bank survey from 2001 cited by Clarke *et al*. indicates that only 12 per cent of the foreign companies having disputes with their Chinese partners used arbitration even once. See Clarke *et al.* 2006, p. 39.
[219] See CIETAC Official Website: http://www.cietac.org/index/aboutUs/47601fd516b2517f001.cms. Last visited 14th of October 2013. In comparison, the ICC Court of Arbitration received between 2008 – 2012 a yearly average of 800 requests for arbitration. See ICC Official Website: http://www.iccwbo.org/Products-and-Services/Arbitration-and-ADR/Arbitration/Introduction-to-ICC-Arbitration/Statistics. Last visited 14th of October 2013.
[220] See Håkansson 1999, p. 166.

tend to have a critical perception about arbitration conducted in the CIETAC.[221] Should foreign parties and their counsels perceive CIETAC arbitration as an attractive method of Sino-foreign dispute resolution, the CIETAC must be able to provide vis-á-vis their Chinese partners an effective and fair mechanism of dispute resolution. In any event, it would seem that the CIETAC currently has, at least amongst Western parties, an image problem.[222]

Generally speaking, Chinese parties tend to prefer Chinese arbitration in comparison to, for instance, ICC arbitration because of the perceived higher costs of overseas arbitration and language barriers.[223] Additionally, the concern regarding the fairness and impartiality of arbitration has been noted to be shared by Chinese businesses regarding overseas arbitration.[224] In particular, China's state-owned enterprises have been identified to possess a tendency to conduct their agreements with their foreign partners under standard-form contracts, which stipulate that disputes are to be resolved by arbitration taking place in China.[225]

Notwithstanding whether the Chinese concerns are justified or not, the referred conflict of interest between foreign and Chinese parties inevitably complicates the choice of the arbitral venue. According to Håkansson, Chinese parties seem to be more comfortable to agree to overseas arbitration in valuable contracts involving large foreign investments. This being said, the majority of Sino-foreign contracts have been noted to provide for CIETAC arbitration.[226]

Chinese arbitration law sets high moral and professional qualifications for being an arbitrator in China. Whereas Chinese judges may be admitted after two years' of experience in legal work after passing the National Judicial Exam, Chinese arbitrators are required to have eight years of legal or

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[221] See Zimmerman 2010; Cohen 2006; Fouchard – Gaillard – Goldman 1999, p. 163 and International Arbitration Survey 2010. It is worth observing that the pool of corporate respondents sharing their perceptions about an arbitral procedure taking place in mainland China was been relatively small (only 9 from 136 respondents). In Peerenboom's view, Western media has played a major part with regard to the general negative portrayal of China. See Peerenboom 2002, pp. 560 – 563.

[222] See Gu 2013, pp. 78 – 79 and Zesch 2012, p. 283. As none of the corporate respondents of the cited questionnaire had ever been subjected to arbitration conducted in the CIETAC, it could be argued that the result of the questionnaire describes more about the prejudicial attitude of the corporate respondents than of the actual quality of arbitration in mainland China. This observation supports the thesis that a concrete need for an objective assessment regarding the choice of submitting to either ICC or CIETAC arbitration in Sino-foreign dispute resolution does exist.

[223] See Gu 2013, pp. 78 – 79. Contrary to Chinese prejudices, the CIETAC's fees have been noted to exceed the fees of ICC and SCC as the value of the dispute arises. See Moser *et al.* 2007, pp. 75 – 76.

[224] See Gu 2013, pp. 78 – 79.

[225] See Håkansson 1999, p. 53. Zimmerman even claims that a Chinese party will not want to arbitrate in any other forum than a CIETAC tribunal at the initial onset of negotiations. See Zimmerman 2010, p. 24.

[226] Ibid, p. 54.

judicial experience or a senior professional title in the field of trade and economics.[227] Foreigners are allowed to serve as arbitrators with more relaxed requirements.[228] However, as the case has been with other former socialist countries, Chinese arbitration commissions maintain closed panel lists from which the arbitrators are appointed. Most of the panelists are Chinese nationals, and the presiding arbitrator has been noted to be Chinese by default.[229] Chinese scholars have justified such restrictions of party autonomy with the immaturity of the Chinese arbitration community.[230] Albeit the amount of panelists has been increased and the appointment criteria gradually loosened, the fact that a CIETAC arbitral tribunal may consist of one, if not three Chinese nationals can be an unpleasant surprise for the foreign party and be understandably perceived as a partial practice.[231] This concern is particularly dire with regard to FIEs[232], which are deemed to be domestic entities under PRC law and may thus lose the opportunity to appoint foreign arbitrators from the CIETAC's international panel.[233]

But is CIETAC arbitration fair and effective? According to statistical data analysed by a CIETAC arbitrator, arbitral awards rendered from CIETAC arbitration have been noted to be *de facto* substantively fair.[234] On the other hand, even if the CIETAC is rendering substantively fair decisions, this in itself does not necessarily mean that the procedures have been conducted in a fair manner. There is, however, little empirical evidence to support allegations of anti-foreign bias amongst Chinese arbitrators.[235] Furthermore, whereas local protectionism infamously plagues the Chinese judiciary to date, Cao has assessed that the location of the CIETAC commissions in the

[227] See Gu 2008, p. 123.
[228] See Art. 13 and 67 of the CAL.
[229] See Gu 2008, pp. 124 – 125 and 137.
[230] See Gu 2013, pp. 106 – 107.
[231] Ibid, pp. 108 – 109. For instance, the Finnish Foreign Ministry recently attempted to obstruct the enforcement of a CIETAC award claiming that the arbitral tribunal, consisting of three Chinese nationals, had been partial and limited the Finnish Foreign Ministry's chances to present oral evidence in the case. Premised on the pro-enforcement bias set towards foreign arbitral awards, the District Court of Helsinki found no grounds for the refusal of the arbitral award. See Ideal Design & Construction Co. Ltd v. Foreign Ministry of Finland. The composition of the arbitral tribunal could be remedied with the use of an arbitration agreement that explicitly requires the presiding arbitrator to be from a third country. This is, however, not a well-known practice, and the CIETAC seems to be reluctant to publish any statistics regarding its use. See Cohen 2006, p. 33. In Zimmerman's opinion, "convincing the neutral arbitrator to rule in your client's favour is the trick" to succeed in CIETAC arbitration. See Zimmerman 2010, p. 23.
[232] Chinese law knows three different types of foreign-invested enterprises. These include a) equity joint ventures, b) contractual joint ventures and c) wholly foreign-owned enterprises. See Chen 2008, pp. 645 – 648 and *infra* Chapter 5.
[233] In addition, the enforcement of a domestic arbitral award in China differs from the treatment of foreign arbitral awards as domestic awards may be subjected to a wider scope of review. See *infra* Chapter 5.4.
[234] According to Cao, in cases involving Sino-US parties the winning percentage of the American parties has been approximately equal to their losing percentage. See Cao 2008, p. 2.
[235] See Zesch 2012, pp. 283 – 293.

capital and the other more developed Chinese cities protects the institution from the influence of local protectionism.[236] Indeed, it is true that researchers of Chinese law typically associate local protectionism with lower-level Chinese courts rather than high-profile arbitration institutions such as the CIETAC.[237]

Again, a disclaimer is in order. It would be somewhat naive to assume that tendencies equally worrisome to local protectionism would be non-existent in CIETAC arbitration. For instance, Jerome A. Cohen, a respected legal scholar and experienced CIETAC arbitrator, has urged for the CIETAC to address the defects that relate to the procedure according to which the arbitrators' hearing the proceedings are chosen, considered biased, and expected confidentiality.[238] Indeed, some practitioners even claim that CIETAC arbitration should be avoided at all costs.[239]

Despite room for improvement thus still exists due to the admitted immaturity of the Chinese arbitration community, it would seem appropriate to conclude that the CIETAC is doing its best to meet the expectations of the international business community.[240] In the author's opinion, the most urgent issues related to CIETAC-administered arbitrations seem to be rather are related to the restrictions set by the Chinese law on arbitration than the CIETAC.[241] Again, because Chinese arbitration law does not explicitly allow separate choice-of-law rules to be applied in proceedings of international arbitration, Chinese arbitral tribunals may not determine the applicable choice-of-law rules. Instead, the choice-of-law rules of the national law in the territory of which the seat of the arbitration is held that become applicable. In conclusion, the Chinese Communist Party has decided, contrary to international practice, to retain the power to determine what choice-of-law rules a Chinese arbitral tribunal may apply. With regard to the fulfilment of the principle of party autonomy, another conclusion would exaggerate the currently non-existent power of the CCOIC

[236] See Cao 2008, p. 3.
[237] See *supra* Chapter 3.2.1.
[238] Cohen has, among others, suggested that the CIETAC should refrain from using its own personnel as arbitrators. See Cohen 2006, pp. 32 – 37.
[239] See Zimmerman 2010, p. 23.
[240] See Zesch 2012, pp. 292 – 293.
[241] See, for instance, *supra* Chapter 1.2 on prohibition of *ad hoc* arbitration in China and Chapter 1.4.1 on the Chinese 'dual-track' regime on arbitration.

and CIETAC with regard to the determination of the choice-of-law rules applied in CIETAC-administered arbitrations.[242]

[242] The CCOIC is mandated to amend the arbitration rules of the CIETAC "in accordance with the Chinese Arbitration Law". See *supra* Chapter 2.2. Despite there is progress towards a society governed by rule of law, China remains a single-party authoritarian state. See *supra* Chapter 3.2.1.

4 The Determination of the Substantive Law in the Absence of the Parties' Agreement

4.1 Under the Arbitration Rules of the ICC

4.1.1 Determination of the Place of Arbitration

When a Request for ICC Arbitration based on a validly concluded arbitration clause is filed, one of the first steps of the ICC Court of Arbitration ("ICC Court") is to determine the place of the arbitration. This is an important preliminary question requiring clarification *inter alia* because the parties' choice regarding the substantive law may be limited by the mandatory provisions of the law of the seat of arbitration.[243] In the absence of the parties' agreement, the place of the arbitration shall be fixed by the ICC Court.[244] The ICC Rules do not provide any explicit guidelines regarding the factors that determine or influence the choice of the place of arbitration. Regarding the *lex arbitri*, the choice of the ICC Court should, however, ensure that the parties and their chosen arbitrators are able to exercise their discretion regarding the arbitration proceedings within the boundaries set by the ICC Rules and *inter alia* the New York Convention. Experienced commentators have listed other contributing factors to include the perceived neutrality of the *forum*, the effectiveness of the ultimate award, the attitude of the local courts, the availability of adequate support services, the parties' choice of the applicable law and the convenience of the parties.[245] Applying these factors, the ICC Court in 2012 selected 92 different cities in 59 countries.[246]

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[243] The number of countries in which an international arbitration could be safely situated used to be considerably smaller because of the prevalence of unfavourable local laws on international arbitration. As a result of the worldwide trend towards modernisation and liberalisation of arbitration laws, this number has increased significantly. Nevertheless, the choice of place of arbitration remains a decision that must be made with care. See Derains – Schwartz 2005, pp. 210 – 211 and Craig – Park – Paulsson 2000, p. 8 and 185. In the author's opinion, the CAL, which is elaborated in this study, remains to be a fairly good contemporary example of a restrictive *lex arbitri*.

[244] See ICC Rules, Art. 18(1). The wording of the provision has been made deliberately in order to stress the created link between the arbitration and a specific jurisdiction. Should the parties' want to agree validly on the place of the arbitration, they should explicitly refer to a city as the place of arbitration instead of a country. See Grierson – Van Hooft 2012, p. 32 and Derains – Schwartz 2005, pp. 211 – 212.

[245] See Grierson – Van Hooft 2012, pp. 118 – 119; Derains – Schwartz 2005, pp. 212 – 215 and Craig – Park – Paulsson 2000, pp. 186 – 189.

[246] The same statistics reveal that the choice of the place of arbitration was left for the ICC Court only in 10 per cent of cases. See ICC Statistics 2012.

4.1.2 Terms of Reference

Once the ICC Court has made the initial decisions regarding the arbitration, the Secretariat of the ICC will transfer the details of the arbitration for the arbitral tribunal.[247] After the chosen arbitrators have received this file, one of the first measures taken by them is to draft a document called "Terms of Reference". This document is an agreement between the arbitral tribunal and the parties, which is drafted in order to keep track of the details of the arbitration and the parties' claims concerning the dispute at hand.[248] The content of the Terms of Reference is stipulated upon Article 23(1) of the ICC Rules, which, among other things, should include remarks concerning the parties' agreement as to the substantive law governing the dispute or else their contentions as to what that law should be.[249]

In the absence of the parties' express or tacit agreement regarding the law applicable to the merits of the dispute, the chosen arbitral tribunal is to search guidance from the chosen rules of arbitration.[250] The ICC Rules contain explicit provisions regarding the arbitrators' inquiry to determine the substantive law. Unless the parties have agreed otherwise, the choice of the arbitral tribunal between the various approaches depends on whether the parties have made an explicit reference regarding the scope of discretion conferred on the arbitral tribunal. Therefore, the following systematisation elaborates the normative content of the ICC choice-of-law rules in correspondence with the scope of discretion given for the arbitrators, beginning from the approach conferring the broadest scope of choice-of-law power available.

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[247] See ICC Rules, Art. 16.

[248] The drawing up of Terms of Reference is one of the principal hallmarks of ICC arbitration: it is performed in all ICC arbitrations. In practice, many experienced arbitrators will draw up a similar document at the beginning of the proceedings even in *ad hoc* arbitrations or arbitrations administered by institutions other than the ICC. See Grierson – Van Hooft 2012, p. 146.

[249] Each arbitrator has his or her own preference as to how to draft Terms of Reference, and there are many different formats of Terms of Reference that manage perfectly well to incorporate the information stipulated by Article 23(1). Ibid, pp. 147 – 149.

[250] It should be emphasised that the parties are free at any point during the arbitration to agree upon the applicable law. In practice, when the dispute has culminated into the point that the parties must seek remedy from arbitration, the chances of finding an amicable solution regarding the substantive law might be very slim. A recalcitrant party is rather more likely to dispute all of the equivocal facts regarding the underlying contract in an attempt to avoid or delay the arbitration proceedings. See Ferrari – Kröll *et al.* 2010, pp. 21 – 22.

4.1.3 The Various Approaches Provided by ICC Rules

First of all, the arbitral tribunal may under the ICC Rules assume the powers of an *amiable compositeur*, if the parties have explicitly agreed on it.[251] This is a so-called equity clause, meaning that the arbitral tribunal is under the discretion of an *amiable compositeur* free to determine the applicable rules of law on the basis of what is 'fair and reasonable' rather than on the basis of law.[252]

If the parties have not explicitly agreed upon conferring such powers to the arbitral tribunal, the ICC Rules will serve as the basis of inquiry regarding determination of the governing law. The provision regarding the determination of the applicable rules of law states:

> The parties shall be free to agree upon the rules of law to be applied by the arbitral tribunal to the merits of the dispute. In the absence of any such agreement, the arbitral tribunal shall apply the rules of law, which it determines to be appropriate.[253]

While the first part of the provision confirms the parties' freedom to determine the applicable rules of law to the merits of the dispute, the second part of the provision directs the arbitral tribunals' inquiry upon the applicable law in the absence of such an agreement. In relation to the second part of the provision, the notions "rules of law" and "determines to be appropriate" call for further interpretation.

According to internationally established arbitration practice, the notion "rules of law", contrary to the notions "the law" or "laws", may also refer to other sources of law besides national legislation.[254] Whereas contemporary national choice-of-law statutes still tend to embrace the approach where only national legislation qualifies as the source of applicable law, modern

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[251] See ICC Rules, Art. 21(3). The notions *amiable compositeur* and *ex aequo et bono* are used interchangeably in both arbitration rules and national arbitration statutes. See Wortmann 1998, p. 103 at fn. 32.
[252] Whereas the notion 'in equity' is obviously prone to several different interpretations, commentators do, however, agree that even an arbitral tribunal deciding the applicable law *ex aequo et bono* must act in accordance with some generally accepted legal principles. In the view of Redfern – Hunter *et al.* this means that the arbitral tribunal should reach its decision based largely on a consideration of the facts and on the provisions of the contract, whilst trying to ensure that these provisions do not operate unfairly to the detriment of one or the other of the parties. See Redfern – Hunter 2009, pp. 227 – 228.
[253] See ICC Rules, Art. 21(1).
[254] See Derains – Schwartz 2005, pp. 234 – 237.

arbitration statutes tend to favour the "rules of law" approach.[255] Other sources of applicable law referred to could be, for instance, the general principles of law, *lex mercatoria* or the UNIDROIT Principles.[256] Thus, the ICC Rules allow for the arbitral tribunal to look beyond a national system of rules, even when the parties do not expressly direct them to do so.[257] In addition, the notion "rules of law" in the context of ICC arbitration has been interpreted to allow for the use of *dépeçage*, i.e. the parties' or their chosen arbitrators' choice of having different laws to govern different aspects of a dispute which may arise between them.[258]

The notion "determines to be appropriate" featured in Article 21(1) of ICC Rules is a manifestation of the direct approach.[259] As in the case of deciding the applicable law *ex aequo et bono*, the broad discretion provided by the direct approach does not, however, imply that the arbitrators may make an arbitrary choice.[260] Ferrari – Kröll *et al.* have assessed some of the possible choices of law, when the arbitrators are vested with the choice-of-law power conferred by the direct approach. These include:

- the substantive law of the seat of the arbitration;
- the substantive law of an unrelated, "neutral" country;

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[255] See, for instance, Rome I Art. 3(1), which refers to "the law" chosen by the parties as the source of the governing law. The "rules of law"- approach became more common in national arbitration statutes after 1985 when UNCITRAL Model Law implemented the approach in its Article 28. Consequently, the countries that later implemented the Model Law as their national arbitration law allow the choice of transnational codifications as the substantive law. Arbitration scholars have been unanimous concerning the recognition of the implicit reference of the phrase to concern transnational rules; national courts have never questioned this interpretation. See Fouchard – Gaillard – Goldman 1999, pp. 801 – 802.

[256] Transnational sources of law may apply in several different forms in connection with a dispute submitted to international commercial arbitration: they could supplement and correct the applicable national law or function as an autonomous source of law. The role of *lex mercatoria*, however, depends on what the applicable choice-of-law rules allow for. See Liukkunen 2013, pp. 209 – 210. Whenever the parties refer to transnational sources of law, the arbitral tribunal is to establish what the parties had in mind when they used a particular expression to describe the rules of law applicable to the dispute. In doing so, they must take into account the continuing linguistic fluctuations and search for the true intention of the parties by going beyond the terms actually used. On this matter and the discussion regarding which rules may qualify as transnational rules, see Liukkunen 2013, pp. 210 – 217 and Fouchard – Gaillard – Goldman 1999, pp. 801 – 806.

[257] See Ferrari – Kröll *et al.* 2010, pp. 294 – 295. Statistics, however, indicate that this power is not *de facto* utilised in a comprehensive scale, as only 3 per cent of the ICC arbitrations conducted in 2012 specified another set of norms than a state law as the applicable law. See ICC Statistics 2012.

[258] Though Lew *et al.* would extend *dépeçage* only to concern arbitration rules which refer to 'laws' in a plural form, a commentary and relevant awards explicitly confirm the allowance of dépeçage in ICC arbitration. See Lew *et al.* 2003, pp. 41 and Derains – Schwartz 2005, p. 234.

[259] See Derains – Schwartz 2005, pp. 239 – 241 and Craig – Park – Paulsson 2000, p. 320. On the direct approach, see *supra* Chapter 2.1.

[260] In order to fulfil its duty under Article 31(2) of the ICC Rules, the arbitral tribunal is obliged to state the reasons, among others, regarding the choice of the substantive law. See Craig – Park – Paulsson 2000, p. 329.

- the most "modern", "commercial" or "developed" law or rules of law;
- combination of the rules found in the national laws of the countries connected to the dispute (the *tronc commun* doctrine); and
- the uniform substantive law conventions.[261]

Arguably the most intuitive choice would be to apply the law of the seat of the arbitration as the substantive law. It has been reasoned that if the parties make no express choice of law but agree to the litigation of future disputes in a particular country, the parties' intention to apply the national law of that country could be inferred from this consensus.[262] Several commentators have, however, opined that such reasoning is dubious even when applied to national court proceedings and does fit even worse in the context of contemporary international arbitration.[263] Thus, the choice of the place of the arbitration should count as nothing more than another general connecting factor, which may be of relevance in the circumstances of the particular case.[264]

The arbitrators may also choose to apply a law that may *prima facie* appear to be completely unfounded for.[265] The grounds for the choice of an unrelated or neutral law may, however, be shrouded by the fact that the arbitrators' analysis involves the balancing of several connecting factors, which combined suggest the application of a neutral law.[266]

The selection of the law that the arbitrators believe to be the most "modern", "commercial" or "developed" has been argued to reflect the truly independent nature of the *voie directe* from any

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[261] See Ferrari – Kröll *et al.* 2010, pp. 297 – 303.
[262] In an award made in Paris in 1976 in ICC Case No. 2735, the arbitral tribunal considered that the choice of applicable law could be inferred from the determination of the seat of the arbitration.
[263] See Redfern – Hunter 2009, p. 233.
[264] See Ferrari – Kröll *et al.* 2010, p. 297 and Lew *et al.* 2003, pp. 415 – 416. An award rendered in London in 1988 stated that "the choice of London as the place of arbitration and English as the language of the contract does not, in itself, indicate an intention of the parties that English law should govern the validity of the agreement to arbitrate." See ICC Case No. 5717. The reasoning of the cited award has been praised to reflect the ideals of modern international arbitration. See Fouchard – Gaillard – Goldman 1999, p. 788.
[265] In an influential ICC Award No. 3540 rendered in 1980, the arbitral tribunal reasoned that "an arbitral clause does not allow the choice of a substantive law to follow from the country where the arbitral tribunal has its seat, since that is merely an indication which itself is insufficient […]; as is, moreover, a contractual prorogation of competence in favor of an ordinary court […], that thus the maxim *qui elegit judicem eleget ius* has been abandoned". In other words, the arbitral tribunal completely excluded the application of the substantive law of the *lex arbitri* in its reasoning.
[266] The connecting factors taken into account could *inter alia* consist of the connection of the country of the applicable law to the parties or the dispute, the place of the business of the parties, the place of performance of the contract or where it had been concluded. In any event, such an analysis typically involves a certain kind of conflicts of law analysis. See Ferrari – Kröll *et al.* 2010, pp. 298 – 299.

conflicts of law analysis.[267] However, Ferrari – Kröll *et al.* note that whereas such an approach does implement the ideals of a truly anational procedure of international arbitration, it puts, in practice, more constraint on the arbitrators' expertise.[268]

The *tronc commun* doctrine is another example of a completely independent approach. The basic idea of the doctrine is to compare the substantive rules of the various countries connected with the dispute and apply them in a parallel manner. In practice, the utilisation of the *tronc commun* doctrine can be difficult, as the application of several, possibly conflicting rules of law not only requires extensive studies of comparative law but also may prove to be virtually impossible due to the incompatibility of the rules. Consequently, the doctrine has been rarely put to practice.[269]

Instead, uniform substantive law conventions have proved to be more successful embodiments of the international principles utilised in international commercial arbitration. Albeit the application of *inter alia* the 1964 Hague Uniform Sales Law or the CISG in an arbitration procedure would not seem to manifest the direct approach very well,[270] arbitrators have been forced to resort to the referred conventions because the requirements for their application were simply met.[271] On the other hand, some ICC arbitral tribunals have also voluntarily invoked to the conventions as the source of governing law, premised on the conventions' embodiment of *lex mercatoria* and international trade usage.[272] For the sake of clarification, it should, however, be noted that the presented list of available choices regarding the governing law is non-comprehensive.[273]

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[267] The same claim is true regarding the application of transnational law, e.g. the generally accepted principle(s) of contract law, UNIDROIT Principles or *lex mercatoria*. See ICC Arbitral Awards Cases No. 11440, 8547 and 3131 respectively.
[268] See Ferrari – Kröll *et al.* 2010, pp. 300 – 301.
[269] Ibid, p. 302.
[270] The application of the uniform substantive law conventions outlines the discretion of the arbitral tribunal to resemble the one exercised by a court of a Contracting State. Ibid, p. 303.
[271] See ICC Interim Award in Case No. 9781; Arbitral Award Case No. 8817; ICC International Court of Arbitration, Arbitral Award Case No. 6076. For a case where the CISG was not applied because the applicability requirements were not met, see ICC Arbitral Award Case No. 6281.
[272] See, for instance, ICC Arbitral Award Case No. 2879.
[273] Other scholars argue that the cumulative application of the different rules of conflict of the countries having a relation to the dispute has been the most frequently used method of reasoning in ICC arbitrations. See Craig – Park – Paulsson 2000, pp. 326 – 327. In Lando's opinion, there are as many approaches to determine the substantive law as there are nationalities, legal backgrounds and attitudes of the arbitrators. See Lando 1991, pp. 140 – 141.

4.2 Under the Arbitration Rules of the CIETAC

4.2.1 Determination of the Place of Arbitration

With its headquarters in Beijing, the CIETAC features sub-commissions in Shenzhen, Shanghai, Tianjin, Chongqing and, as a result of the CIETAC's latest effort to internationalise, Hong Kong SAR.[274] Late developments have, however, complicated the choice of the arbitral venue in CIETAC-administered arbitrations as the CIETAC has been since mid-2012 been in a brawl between its sub-commissions in located in Shenzhen and Shanghai. As a result, the Shenzhen and Shanghai sub-commissions declared their independence from the CIETAC and *inter alia* changed their names and stipulated arbitration rules of their own.[275] In consequence, parties have been advised to refrain from drafting arbitration clauses that refer to either CIETAC Shanghai or Shenzhen as the place of arbitration.[276]

The choice of the place of arbitration regarding CIETAC arbitration *prima facie* appears relatively simple. The parties may freely agree upon the place of arbitration.[277] When the parties have not agreed on the place of arbitration or their agreement is ambiguous, the place of arbitration shall be the domicile of CIETAC or its sub-commission/centre administering the case.[278] This being said, the amendments made to Article 2(6) of the CIETAC Rules lead to the default administration of CIETAC Beijing in the absence of the parties' agreement and, consequently, for the place of the arbitration to be in Beijing in the absence of party instructions.[279] It has been argued that the cumulative effect of these revisions was the reason for the discontent and withdrawal of the Shanghai and Shenzhen sub-commissions from CIETAC.[280] Albeit Article 33(4) of the CIETAC Rules does allow for hearings also to be held abroad, this provision is insignificant in relation to the choice of the place of the arbitration.

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[274] See the Official Websites of the CIETAC. Last visited 22nd of January 2014. Because of the multi-jurisdictionality of the People's Republic of China, arbitration proceedings between parties from mainland China and Hong Kong SAR, Macao SAR and Taiwan are considered to be 'foreign-related' instead of domestic ones. See Tao 2012a, p. 98.
[275] See Leung 2013, p. 2.
[276] Ibid, pp. 8 – 9. Chinese courts have taken an inconsistent approach with regard to the validity of arbitration agreements and the enforceability of awards in connection with the Shenzhen and Shanghai sub-commissions. Even though the SPC has acknowledged the potential problems caused by the referred breakaway, it has not issued any express clarification. See D'Agostino *et al*. 2014.
[277] See Art. 7(1) of the CIETAC Rules.
[278] See Art. 7(2) of the CIETAC Rules.
[279] See Choong 2014, p. 2.
[280] Ibid.

The CAL will apply as the *lex arbitri* when the parties have explicitly chosen it or the seat of the arbitration is in mainland China. Most importantly, in the absence of the parties' agreement, the CAL will also apply if a Chinese tribunal has been seized. Thus, the applicability of the CAL may be only avoided by either explicitly choosing a different *lex arbitri* or a place of arbitration outside of China provided that the applicable Chinese law entitles the parties to submit their dispute to a foreign jurisdiction.[281]

The latter option, the CIETAC's power to opt for a place of arbitration outside mainland China, is an addition made in the latest revision of the CIETAC Rules.[282] This could represent a significant change to earlier practice, given that the choice of the seat of arbitration *inter alia* determines the law governing the arbitration procedure. Because the clause is relatively new, there is no praxis regarding the application of the provision. Consequently, the practical significance of the addition remains to be seen. On the one hand, it has been assessed that the revised Article 7(2) of the CIETAC Rules is explicitly meant to bring about the possibility of a CIETAC arbitration having a non-Chinese law govern the arbitral proceedings. By doing so, CIETAC could appear as a more flexible and attractive venue for arbitration in the eyes of foreign parties.[283] This being said, it has been advised that the parties should choose the seat on their own rather than to rely on the CIETAC's discretion.[284]

While in theory the choice of a foreign procedural law is thus now possible also in CIETAC arbitration, it is hard to understand why anyone would like to do so. Such an arrangement would *de facto* subject the parties and the arbitral tribunal to two procedural laws, i.e. that of the foreign *lex arbitri* and the provisions of the law of the seat of arbitration to the extent of mandatory rules of law.[285] Should the parties' motive for choosing a foreign procedural law be the avoidance of the

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[281] See Tao 2012a, pp. 108 – 109. The latter reservation is due to the 'dual-track' system of Chinese arbitration, which prohibits purely domestic (Chinese) parties from conducting arbitration outside the People's Republic of China. Conversely, the dispute must be classified as 'foreign' or 'foreign-related' in order to opt for these choices. For more, see *supra* Chapter 1.4.1.

[282] Article 7(2) of the CIETAC Rules stipulates that the "CIETAC may also determine the place of arbitration to be another location having regard to the circumstances of the case."

[283] See Lu 2012, p. 305.

[284] See Zesch 2012, p. 302.

[285] With the exception of the CIETAC venue located in Hong Kong SAR, the mandatory rules of Chinese law become necessarily applicable in the sheer majority of CIETAC arbitrations as they are situated in mainland China, and thus subject to the Chinese *lex arbitri*. See Redfern – Hunter 2009, pp. 184 – 185.

mandatory rules of Chinese law, avoiding CIETAC arbitration is advisable in order to ensure the enforceability of the rendered award.[286]

4.2.2 Limitations of Party Autonomy

When foreign-related arbitration and litigation are concerned, the principle of party autonomy is accepted as the rule of thumb of Chinese law. Conversely, Chinese law does not allow for the parties to choose the governing law in non-contractual matters nor purely domestic contracts, or when application of the law of another country would be contrary to the public interest of the People's Republic of China.[287] As a consequence of these restrictions, it would seem appropriate to clarify the situations related to foreign-related contractual relationships where the application of Chinese law is demanded by the mandatory rule of PRC law before the choice-of-law methodology applied in CIETAC arbitration is further elaborated.

Article 126(2) of the Chinese Contract Law stipulates that the establishment of wholly foreign-owned enterprises, Sino-foreign equity and cooperative joint ventures, and Sino-foreign contracts for the exploitation of mineral resources within the territory of China shall be governed by PRC law. Rules and regulations given by the Chinese authorities explicitly confirm that Chinese law is to be *inter alia* applied to the resolution of disputes arising from these types of contracts.[288]

In other words, if the subject matter of the underlying contract falls into one of the categories elaborated by Article 126(2) of the CCL, the parties or their chosen arbitrators should always choose Chinese law to govern the underlying contract. Should another law be chosen, the arbitral tribunal risks rendering an unenforceable arbitral award. This conclusion is supported by a recent Interpretation of the Supreme People's Court, which states that "where the laws of the People's Republic of China do not explicitly specify that the parties may choose the law applicable to a

[286] See Tao 2012a for the same conclusion regarding the mandatory nature of the CAL, p. 107.
[287] See CCL Art. 126(1); GPCL Art. 145(1); LAL Art. 3 and Liang 2012, p. 79.
[288] Article 12 of SC Rules 2001 states that "the conclusion, validity, interpretation, and performance of a joint venture contract, and the resolution of disputes arising thereunder shall be governed by the laws of the People's Republic of China"; Article 55 of the MOFCOM Rules 1995 states: "the preparation, effectiveness and implementation of a cooperative joint venture contract and the resolution of disputes arising thereunder shall be governed by the laws of the People's Republic of China".

foreign-related civil relation but the parties yet decide to do so, the people's courts will hold such choices as invalid".[289]

The Supreme People's Court later expanded the mandatory application of Chinese law to other FIE-related contracts as well by a now-abolished judicial Interpretation.[290] A Chinese court recently refused to enforce an award based on the referred interpretation. The case was about the enforcement of a foreign arbitral award that related to a share purchase agreement of a Chinese-foreign equity joint venture involving parties from the P.R. China and a foreign country. The parties had included a choice-of-law clause in their underlying contract that stipulated the substantive law to be another than Chinese law. When the foreign party attempted to enforce the given award in a Chinese court, the court refused to do so because the SPC Interpretation 2007 demanded the mandatory application of Chinese law.[291]

As of April 2013, the SPC Interpretation 2007 has been abolished and thus no longer remains a binding source of law. As the SPC is likely to issue a new judicial interpretation in near future that could plausibly reinstate these rules, the application of the law of the PRC as the substantive law regarding all FIE-related contracts is advisable in order to ensure the enforceability of the rendered award in Chinese courts.[292]

4.2.3 The Limited Choice-of-Law Power of CIETAC Arbitrators

Albeit neither the CIETAC Rules nor Chinese law impose *de jure* limitations to the choice-of-law power of CIETAC arbitrators, CIETAC's choice-of-law methodology, which, by default, directs the arbitrators to apply the rules of private international law of the *lex arbitri,* ensures that the arbitrators' discretion to choose the substantive law in CIETAC arbitration is *de facto* limited.

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[289] See SPC Interpretation 2013, Art. 6.

[290] Article 8 of the SPC Interpretation 2007 extended the mandatory application of Chinese law to (1) contracts of transfer for shares of Chinese-foreign equity joint ventures; (2) Chinese-foreign contractual joint ventures, or wholly foreign-owned enterprises; (3) contracts for operation by a foreign natural person, legal person, or other organisation of Chinese-foreign equity joint ventures or contractual joint ventures formed within the territory of China; (4) contracts to purchase by foreign natural person, legal person, or other organisation the equity rights of the shareholders of non-foreign investment enterprises within the territory of China; (5) contracts to purchase by foreign natural person, legal person, or other organisation the newly issued shares of non-foreign invested limited liability company or company limited by shares within the territory of China; and (6) contracts to acquire by a foreign natural person, legal person, or other organisation the assets of non-foreign invested enterprises within the territory of China.

[291] Unfortunately, no published translation of the case particulars seems to be available. The description regarding the case particulars is based on a lecture held by SHEN Wei, 11th of September 2013.

[292] See *infra* Chapter 4.2.3.

The CIETAC Rules have for a long time contained a somewhat ambiguous provision titled "Making of the Award", which guides the arbitral tribunals' inquiry regarding the sources of law which can be used to determine the applicable law; the provision strongly resembles the position taken in the Chinese Arbitration Law.[293] This article states:

> The arbitral tribunal shall independently and impartially make its arbitral award on the basis of the facts, in accordance with the law and the terms of the contracts, with reference to international practices and in compliance with the principle of fairness and reasonableness.[294]

The CIETAC Rules include no explicit remarks regarding the arbitrators' possibility to assume the powers of *amiable compositeur* or decide the applicable law *ex aequo et bono*. While some commentators have assessed the provisions' reference to 'fairness and reasonableness' to in theory give arbitrators the ability to decide cases according to principles of equity,[295] in practice this discretion may be exercised only in rare occasions. This is because of the motley collection of conflict rules provided by PRC law, which exclude virtually all imaginable situations in which the arbitrators' discretion may be exercised.[296] In any event, should the parties' still wish to confer the arbitrators' the power to act as *amiable compositeurs* in CIETAC arbitration, they should do so expressly.[297]

Another observation regarding the application of transnational law should be made at this point. Premised on international arbitration practice, the reference of both Article 47(1) of the CIETAC Rules and Article 7(1) of the CAL to the 'law' to would *prima facie* seem only to allow the arbitrators to choose the law of a state as the governing law.[298] Indeed, the commentary on the issue

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[293] CAL Art. 7 stipulates that "[a]rbitration shall be made based on true facts and relative laws to give out a fair and reasonable settlement for parties concerned."
[294] See Article 47(1) of the CIETAC Rules.
[295] See Redfern – Hunter 2009, p. 228. Because the applicable law and the principles of equity are occasionally mutually exclusive, a question arises as to which has priority and is to be applied in determining a dispute. The well-established position in China is that the law as selected by the parties and recorded in their arbitration agreement will be applied without equivocation. When the selected law is silent on a particular point, the arbitral tribunal will apply international practice and the principles of equity. See Tao 2012a, pp. 113 – 116.
[296] In Chi's view, the lack of circumstances in which the arbitrators may exercise their discretion *ex aequo et bono* results in a *de facto* prohibition of 'in equity' decision-making in Chinese arbitration. See Chi 2011, p. 271.
[297] As explained *supra* in Chapter 4.1.3, the requirement of an express choice stems from international arbitration practice.
[298] See *supra* Chapter 4.1.3.

by leading Chinese scholars confirms such a conclusion.[299] Should the parties opt for the application of supranational rules under the Chinese doctrine of private international law, scholars recommend incorporating transnational law as part of the underlying contract rather than referring to it as the substantive law.[300] Albeit the limited scope of application of supranational law under the Chinese doctrine has been *de lege ferenda* criticised as unnecessarily restrictive,[301] the referred practice, based on the GPCL, remains to stay.[302]

A cited CIETAC award illustrates the status of transnational law under the Chinese private international law approach. The award was about an international sales contract between a Chinese party and a Korean party. The parties did not choose the substantive law and Korea was neither a party to the CISG by the time of arbitration.[303] The claimant requested the tribunal to apply the UNIDROIT Principles, but the tribunal rejected this application and decided to apply Chinese contract law pursuant to the closest connection doctrine. The tribunal held that although UNIDROIT Principles did qualify as "international practices" as meant by Article 47(1) of the CIETAC Rules, the UNIDROIT Principles are only to be applied in the absence of relevant rules of the applicable domestic law pursuant to Article 142(3) of the GPCL. As Chinese contract law contained rules to settle the dispute, no justification to resort to "international practices" existed.[304]

The acceptance of *dépeçage* in China has only little commentary on it. Albeit the LAL does not contain any explicit reference to *dépeçage*, the doctrine has been well accepted in Chinese legal texts.[305] According to Tu's analysis, it seems that *dépeçage* could be accepted to a limited extent in

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[299] This is not to say that Chinese courts would not have applied supranational rules regardless of what the Chinese doctrine allows for. For instance, in cases Fayau v. Wujin International Trade Co. *et al.*.; Shanghai Lansheng Corp. v. Shanghai Branch of OCBC Bank and Citibank China; APL Ltd v. Feida Electrical Apparatus Co. et al**,** and Xiamen Trade Co. v. Lian Zhong (Hong Kong) Co., the court allowed the application of supranational law. See Xiao – Long 2009, pp. 199 – 200.
[300] Ibid, p. 201.
[301] Ibid, pp. 202 – 203.
[302] Article 142(3) of the GPCL states: "International practice may be applied on matters for which neither the law of the People's Republic of China nor any international treaty concluded or acceded to by the People's Republic of China has any provisions."
[303] See *infra* Chapter 5.2 regarding the Chinese exclusion of the indirect application of the CISG.
[304] See CIETAC Award 2007 and also Chi 2011, pp. 274 – 275. Interestingly, Asian countries seem to be relatively unanimous in connection with the refusal to recognise the UNIDROIT Principles as the substantive law. See Chi 2010, p. 8. On the other hand, the incorporation of the UNIDROIT Principles as contract terms seems to be somewhat unproblematic. Ibid and *supra* fn. 300.
[305] Under the principle of party autonomy, the parties may agree to choose the law applicable to the contract. According to Zhang's reasoning, nothing thus indicates that the parties may not choose different laws to govern different parts of the contract. See Zhang 2011, pp. 121 – 122.

China as far as the issue of governing law for a contract is concerned.[306] However, presumably because of the *de facto* arbitrators' limited discretion regarding the choice of the substantive law under the Chinese choice-of-law rules, the question whether the arbitrators may under Chinese law choose different laws to govern different aspects of the dispute remains unsettled.[307]

Before the introduction of the latest revision of the CIETAC Rules of Arbitration, the CIETAC Rules lacked explicit provision(s) that would direct the arbitrators' inquiry regarding the determination of the substantive law in the absence of the parties' agreement. The new Article 47(2) at least partially rectifies this defect. It states:

> Where the parties have agreed on the law as it applies to the merits of their dispute, the parties' agreement shall prevail. In the absence of such an agreement or where such agreement is in conflict with a mandatory provision of the law, the arbitral tribunal shall determine the law as it applies to the merits of the dispute.[308]

The CIETAC Rules thus now explicitly confirm the parties' power to choose the substantive law. The latter part of the provision, however, simply confirms the existing doctrine, which does not provide the arbitrators with any unequivocal guidance regarding the methodology to determine the substantive law. Premised upon international arbitration practice, the arbitrators' are perceived to be responsible to determine the law governing the merits of the dispute in the absence of the parties' agreement.[309] The confirmation of the arbitrators' obligation to determine the substantive law in the absence of the parties' agreement thus is, in the author's opinion, rather trivial.

The arbitrators' explicit duty to override a parties' choice-of-law clause, which conflicts mandatory provisions of the law, arguably counts for larger importance. Generally speaking, the arbitral tribunal is bound to follow the parties' instructions because their powers are derived from the parties' agreement. Consequently, arbitrators in general are very reluctant to deviate from the parties' choice regarding the application of the substantive law.[310] Cordero-Moss has argued that the arbitral tribunal could be bound to disregard the parties' choice with regard to the substantive law

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[306] See Tu 2011, pp. 673 – 674.
[307] See Zhang 2011, p.120 and Tu 2011, p. 673.
[308] See CIETAC Rules, Art. 47(2).
[309] See Fouchard – Gaillard – Goldman 1999, p. 865.
[310] See Bermann – Mistelis 2011, p. 1 and Cordero-Moss 2005, p. 2.

when it is in contradiction with the public policy (*ordre public)* of the otherwise applicable law[311] or, alternatively, with another contractual regulation made by the parties themselves.[312] As elaborated *supra* in Chapter 4.2.2, Chinese law imposes a number of limitations on party autonomy. Thus, the arbitrators explicit duty under Article 47(2) of the CIETAC Rules to disregard a choice-of-law clause, which contradicts with the mandatory provisions of law, is seemingly a direct reference to the limitations imposed by the *lex arbitri.*[313]

In conclusion, the revised Article 47(2) of the CIETAC Rules would not seem modify the pattern of reasoning to determine the substantive law applied in CIETAC arbitration, but instead functions as a mere codification of the established practice. As the CIETAC Rules do not provide the arbitrators' any methodology to determine the law applicable to the merits of the dispute, the arbitral tribunal must turn to the law of the seat of arbitration for supplement.[314] Again, this approach is consistent with the jurisdictional theory of private international law.[315] As concluded *supra* in Chapter 4.2.1, the *lex arbitri* applied in CIETAC arbitration has virtually always turned out to be the law of the People's Republic of China.

Although the Chinese Arbitration Law and Chinese Civil Procedure Law ("CPL") are the most pertinent Chinese laws in the field of foreign-related arbitration, neither of them provides operable conflict of laws rules. This vacuum is thus fulfilled by the Contract Law of the People's Republic of China enacted in 1999 ("CCL"), the General Principles of the Civil Law of the People's Republic of China as amended in 2009 ("GPCL") and the Law on the Applicable Laws in Foreign-Related Civil Relations of the People's Republic of China adopted in 2010 ("LAL"). These three laws all stipulate that in the absence of parties' choice, "the law that has the closest connection with the contract" shall be applied. Additionally, Article 41 of the LAL adds the law of the habitual

[311] The notion of the 'otherwise applicable law' is a reference to the law chosen by the parties' themselves. See Bermann – Mistelis 2011, pp. 1.
[312] See Cordero-Moss 2005, p. 2.
[313] See Lu 2012, p. 314.
[314] Nothing prevents the parties from agreeing upon the application of a more modern choice-of-methodology. However, this observation is seemingly only of theoretical value. See *infra* Chapter 5.3.
[315] See *supra* Chapter 2.1.

residence of the party whose fulfilment of obligations can best reflect the characteristics of this contract as a connecting factor.[316]

While some ambiguity does exist regarding the precise scope of application of the closest connection doctrine, it has established its status as the most prominent conflicts rule of Chinese private international law.[317] Originally, the closest connection rule was adopted as a conflicts rule in the field of contracts. Its application was extended to cover the discipline of private international law with the introduction of the now-abolished FECL in 1985.[318] Generally speaking, the closest connection doctrine is perceived as a simple and flexible method of choice-of-law methodology, which explains its popularity in national choice-of-law statutes worldwide.[319] Most importantly, the CIETAC arbitrators, too, have confirmedly resorted to the closest connection doctrine in their reasoning.[320]

The vagueness and generality of the said laws has left the concrete application of the Chinese closest connection doctrine undefined. In China, such a manner of law-making is common.[321] The NPC's Standing Committee established a system for the "interpretation of laws" in 1981 as an attempt to clarify the mandate of the different law-making organs.[322] Premised on this system, the Supreme People's Court has been given the mandate to issue various types of judicial documents that concern the concrete application of the law in the adjudicative work of the courts, typically referred to as judicial interpretations.[323] In practice, the law-making role of the SPC has been

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[316] See Chi 2011, p. 272. In international comparison, the (a) habitual residence of the parties, (b) places of businesses of the parties and (c) the place of the characteristic performance have been noted to the factors that are taken into account in the closest connection test. With regard to disputes submitted to international arbitration, the parties' choice of the place of arbitration or the nationality of the arbitrator may also carry weight. See Lando 1991, p. 143.

[317] See Art. 5(1) of the FECL; para. 4 of part 2 of the SPC 1987 Interpretation on the FECL; Art. 145(2) of GPCL; Art. 126(1) of CCL; Art. 5 of the SPC Interpretation 2007; and Art. 41 of LAL. The "closest connection" test has been established in all of these provisions.

[318] See Liang 2012, p. 77; Tu 2011, pp. 678 – 679 and Yu *et al.* 2009, pp. 424 – 427.

[319] See Saarikivi 2008, p.65.

[320] See CIETAC Award 2004.

[321] See Peerenboom 2002, pp. 251 – 252.

[322] In fact, the NPC's Standing Committee, the SPC, the State Council and even the standing committees of local people's congresses all possess the power to issue interpretations and local regulations. See Håkansson 1999, pp. 24 – 25. One of the peculiarities of the Chinese normative hierarchy is that all of the referred provisions, though they stipulate on the one and same issue, are effective legislation. A Chinese court does not possess the power to strike down any of these provisions. Instead, this power has been left solely for the issuing authority. In order to determine the applicable provision, the courts or arbitrators must by means of interpretation decide which one of the possibly conflicting provisions should prevail. See Chen 2011, pp. 148 – 149.

[323] Regarding private international law, relevant provisions has been incorporated in the SPC Opinions 1988 (abolished); SPC Interpretation 2007 (abolished), and the SPC Interpretation 2013 (effective).

considered larger than first envisioned, as the SPC's extensively formed interpretations or "official opinions" often are more detailed than the laws themselves. Due to the interpretations' role as 'gap-fillers', the SPC's judicial interpretations have been determined to be the most important supplementary sources of law despite their ambiguous status in China's normative hierarchy. In fact, the proper enforcement of Chinese laws is arguably impossible without them.[324]

According to renowned Chinese scholars of private international law, the closest connection doctrine is not a single rule to be applied at the arbitrators' discretion. Instead, the closest connection method facilitates the arbitrators' to determine the place of the characteristic performance of the contract.[325] To date, an interpretation of the Supreme People's Court issued in 2007 has provided the basis of inquiry for both Chinese courts and arbitrators respectively. This judicial interpretation divided foreign-related contracts into 17 general types, and designed 19 choice-of-law rules to deal with each of these types respectively.[326] The notion of "characteristic obligation" has thus been determined on the basis of fixed conflict rules for different kinds of contracts.[327] Where the disputed case belonged to one of the types of contracts provided for by the SPC Interpretation 2007, the court or arbitral tribunal was facilitated to apply the designated conflict rule directly; only if the subject matter of case did not belong to one of these categories, the court or arbitrators would be able to exercise their discretion *in casu*.[328] Finally, the SPC Interpretation 2007 also included an 'escape clause', the rationale of which was to avoid results leading to 'unreasonable' choice, allowing for the arbitrators' to apply the law of the country, which obviously has the most significant relationship with the underlying contract.[329]

When the substantive law had been successfully identified, the judge or arbitrator may still need to identify the exact rule(s) of that law to settle the dispute. This is due to the fact that the "applicable law" generally refers to the state law system as a whole. At this point, the Chinese choice-of-law doctrine allows for the judges and arbitrators to exercise their own discretion. In most cases, the

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[324] See Tao 2012a, p. 43; Peerenboom *et al.* 2010, p. 56; Chen 2008, p. 202; Moser *et al.* 2007, p. 50 and Håkansson 1999, pp. 24 – 25.
[325] See Yu *et al.* 2009, pp. 427 – 430.
[326] See SPC Interpretation 2007, Art. 5(2).
[327] See Tu 2011, p. 678.
[328] See Yu *et al.* 2009, p. 431.
[329] See SPC Interpretation 2007 Art. 5(3) and Tu 2011, p. 679.

dispute can be settled upon the completion of the Chinese choice-of-law pattern.[330] Nonetheless, Chinese commentators did identify defects from the SPC Interpretation 2007. These were related to the difficulties regarding the determination the correct conflict rule in complicated contracts, and the extension of the presumptory rules only to the field of contracts and maintenance.[331]

As discussed *supra* in Chapter 1.3, recent developments have further complicated the task to make proper legal dogmatic research with regard to the normative content of the Chinese conflicts of law regime. Soon after the enactment of the LAL, the SPC declared that any earlier interpretations that may conflict with the LAL are not to be applied.[332] As of 8th of April 2013, the SPC Interpretation 2007 has been abolished, making the SPC Interpretation 2013 on the LAL the sole binding supplementary source of law with regard to Chinese rules of private international law.[333] The said development is apparently related to the latest clean-up of the Legislative Affairs Commission of the National People's Congress' Standing Committee.[334]

As Article 41 of the LAL only provides the methodology to determine the substantive law, the question remains: how should the Chinese courts or arbitral tribunals determine the applicable conflict rule in the *prima facie* absence of valid presumptory rules? The author has conceived two possible scenarios premised on this development. On the one hand, the absence of binding presumptory rules could result in the increased choice-of-law power of the arbitrators and thus an arbitration procedure that reflects the principle of party autonomy far better than under the earlier legal state. On the other hand, the presumptory rules of the SPC Interpretation 2007 could still contribute to the arbitrators' discretion as *de facto* source of conflict rules.

No recent Chinese commentaries, relevant judicial practice or published CIETAC arbitral awards regarding the application of the LAL premised on the SPC Interpretation 2013 seem to be available to date. Consequently, an attempt to find the correct answer to this question is a seemingly insurmountable problem. Being a researcher of a legal system of an essentially foreign origin in this matter, the conclusions of this study regarding this matter should be approached with caution.

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[330] See Chi 2011, p. 274.
[331] See Yu *et al.* 2009, pp. 430 – 431.
[332] See LAL Notice 2010, Section IV.
[333] See Interpretation of the Supreme People's Court on Several Issues Concerning Application of the Law of the People's Republic of China on Choice of Law for Foreign-Related Civil Relationships, as adopted by the Judicial Committee of the Supreme People's Court on 10th of December 2012 and effective from 7th of January 2013.
[334] See http://news.xinhuanet.com/english/china/2013-04/23/c_132334248.htm. Last visited 10th of January 2014.

Based on the established Chinese reliance to presumptory rules under the closest connection doctrine and the SPC's function as a gap-filler under the Chinese doctrine of law-making, the author suggests that the Supreme People's Court is about to introduce a new judicial interpretation that will more or less reinstate the normative content of the now-abolished SPC Interpretation 2007.[335] Until a new judicial interpretation is issued, the author considers it possible that the conflict rules of the SPC Interpretation 2007 could continue to contribute the judges' and arbitrators' reasoning regarding the determination of the substantive law as a *de facto* source of law, although it no longer is a legally binding source of law.[336]

The said conclusion finds support from judicial practice. Professor HE Qisheng, an expert of Chinese private international law and international commercial arbitration, has assessed that "the Chinese choice-of-law pattern has not undergone through any dramatic changes after the enactment of the SPC Interpretation 2013, especially in regard to the field of international arbitration".[337] The author finds this statement rather surprising as the exact normative content of the Chinese choice-of-rules is seemingly ambiguous. It might, in fact, very well be that the abolishment of the previous SPC Interpretation 2007 has changed this situation. On the other hand, the interpretative authority of the Chinese courts has been noted to be "extremely limited".[338] Perhaps the Chinese judges' and, as an analogy, the arbitrators' forbearance to exercise more discretion with regard to the determination of the substantive law under the Chinese choice-of-law rules is, after all, just the logical outcome of the limited interpretative power of Chinese legal professionals.[339] In any event, the application of the Chinese choice-of-law rules is, in the author's opinion, subject to legal uncertainty until a new judicial interpretation is issued.

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[335] The cited proposal of the Legislative Affairs' Commission, which advises to "further regulate and regularly improve" the formulation of judicial interpretations, arguably supports a such conclusion. Ibid.

[336] Despite its ambiguity as a source of law after the enactment of the LAL in 2010, Chinese scholars have confirmed that the SPC Interpretation 2007 was a source of presumptory rules at least until its formal abolishment in April 2013. See *supra* fn. 45. This was possible because the LAL Notice forbade the application of only such conflict rules that contradict with the LAL. Conversely, as the SPC Interpretation 2013 did not introduce any new presumptory rules, it would seem fair to deduce that the SPC Interpretation 2013 was neither an obstacle apply the presumptory rules featured in the earlier judicial interpretations, such as the SPC Interpretation 2007. See LAL Notice, Section IV. Finally, the weakness and immaturity of the Chinese judiciary and arbitration community supports the thesis that a scenario, in which Chinese judges' and arbitrators' continue to apply to a now-abolished source of law as a basis of their reasoning, is possible. See *supra* Chapter 3.2.1.

[337] Correspondence with HE Qisheng. Conducted 8th of November 2013.

[338] See, for instance, Peerenboom 2002, pp. 316 – 320 and 421..

[339] Such an analogy is at least possible, because the same choice-of-law rules apply to both Chinese litigation and arbitration. See Chi 2011, p. 275. The admitted immaturity of the Chinese arbitration community supports a such thesis. See Gu 2013, pp. 106 – 107.

The question regarding the factors contributing to the arbitrators' discretion remains so far unanswered by Chinese scholars of private international law.[340] In the case of Chinese courts, Yu *et al.* argue that an increased discretion has led to an unsatisfactory tendency to apply Chinese law (*homeward trend*).[341] Albeit a higher standard of reasoning could be rightly expected from an expert tribunal of arbitrators, it might not be an overstatement to deduce that CIETAC arbitrators may, too, have had a tendency to apply Chinese law whenever possible. As explained, the Chinese GPCL has been interpreted in a manner that only allows for the supplementary application of transnational law, even in proceedings of international arbitration.[342] Furthermore, as the Chinese rules of private international law apply to both Chinese litigation and arbitration and the Chinese arbitration regime remains to be admittedly immature,[343] such an assumption is, in the author's opinion, justifiable.

4.3 Comparing the Choice-of-Law Methodology Applied in ICC and CIETAC Arbitration

As the proverb knows, a picture is worth a thousand words.[344] Thus, the researcher has considered it appropriate to demonstrate the arbitrators' reasoning under the ICC and CIETAC choice-of-law methodology with images hopefully of illustrative value. The following descriptions function under the assumption that the applicable *lex arbitri* has been determined according to the default scenario, i.e. the ICC Rules are exercised under a neutral, non-restrictive *lex arbitri*, and the CIETAC Rules under the Chinese Arbitration Law.

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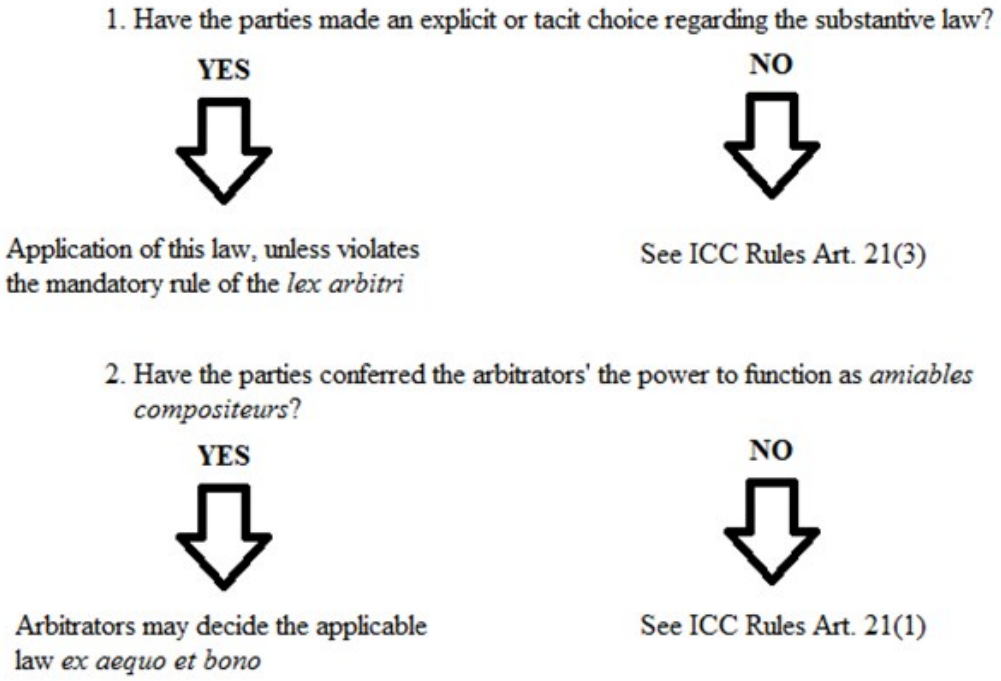
[340] Yu *et al.* do not specify any factors that might contribute to the case-by-case analysis conducted in the absence of an appropriate conflict rule. In any event, the application of presumptory conflict rules have ensured that the courts have not been allowed to exercise their own discretion but in exceptional circumstances. See Yu *et al.* 2009, p. 430.
[341] Ibid, pp. 434 – 436.
[342] See GPCL Art. 142(3) and CIETAC Award 2007.
[343] See *supra* fn. 339.
[344] According to the Oxford English Dictionary, the coining of the proverb is attached to a certain J. K. Paulding in his works 'The New Mirror for Travellers; and Guide to the Springs. By an Amateur' published in 1828. Most interestingly, the proverb has been apparently inaccurately attached also to be of Chinese or Japanese origin. Whatever the case may be, consensus does exist regarding the content of the wisdom: a picture conveys far more than words. See http://www.oed.com. Last visited 5th of November 2013.

The Choice-of-Law Methodology Applied in ICC Arbitration



The choice-of-law methodology applied in ICC arbitration may be summarised as follows. If the parties have agreed upon the substantive law in their underlying agreement, it shall be respected unless it violates the mandatory rule of the *lex arbitri*.[345] If the parties have explicitly agreed upon conferring the arbitral tribunal the discretion to decide the substantive law in equity, the arbitrators may do so. In the absence of the parties' agreement, the arbitrators' will determine the applicable rules of law as they see appropriate.[346]

[345] Albeit the vast majority of awards are performed voluntarily, arbitrators would be foolish to disregard the mandatory rules, or public policy, of the country of enforcement, if it can be identified in advance. Should the arbitral tribunal render an award contrary to the mandatory rules of the country of enforcement, they risk rendering a practically unenforceable award. See Redfern – Hunter 2009, p. 622, Ferrari – Kröll *et al.* 2010, p. 334 and Bermann – Mistelis 2011, pp. 12 and 77.
[346] See *supra* Chapter 4.1.3.

The Choice-of-Law Methodology Applied in CIETAC Arbitration

1. Have the parties made an explicit or tacit choice regarding the substantive law?

YES

Application of this law, unless violates the mandatory rule of Chinese law

NO

See CIETAC Rules Art. 47(1) and (2)
CAL Art. 7

2. Consideration of a) the facts,
b) the law and terms of contract,
c) international practices and
d) the principle of fairness and reasonableness.

"[T]he arbitral tribunal shall determine the law as its applies to the merits of the dispute."

3. No unequivocal guidance; search for supplementary conflict rules from the *lex arbitri.*

See CCL Art. 126(1);
GPCL Art. 145(2);
LAL Art. 41;

4. "The law that has the closest connection with the contract shall apply."

5. The established doctrine of Chinese private international law directs to determine the place of the characteristic performance.

See SPC Interpretation 2007 Art. 5(2)

6. Does the SPC Interpretation 2007 include a conflict rule applicable to the merits of the dispute?

YES

Application of the law determined by the conflict rule

NO

The arbitral tribunal may exercise its discretion to determine the substantive law

The methodology to determine the law applicable to the merits of the dispute in CIETAC arbitration represents the other extreme regarding the arbitrators' discretion, and may be summarised as follows: If the parties have agreed upon the substantive law in their underlying agreement, it shall be respected unless it violates the mandatory rule of Chinese law.[347] In the absence of the parties' agreement, the arbitral tribunal must use the choice-of-law rules of the *lex arbitri* due to the absence of such rules in the CIETAC Rules. The Chinese rules of private international law facilitate the arbitral tribunal to apply the closest connection doctrine, under which the presumptory conflict rules provided by PRC law are applied. Only if the subject matter of the underlying contract does not fit in the categories elaborated in the SPC Interpretation 2007 or the applicable system of law pointed out by the conflict rule does not provide an unequivocal solution, the arbitral tribunal may exercise its own discretion to determine the substantive law.[348]

Albeit the earlier descriptions regarding the choice-of-law methodology applied in ICC and CIETAC arbitration are illustrative, they, however, fail to capture all of the aspects in relation to the arbitrators' discretion. The next chart will compare the available techniques to determine the substantive law and the available sources of law in ICC and CIETAC arbitration. This chart illustrates well how limited the actual choice-of-law power of CIETAC arbitrators is compared to ICC arbitrators.

[347] See *supra* Chapter 4.2.2 and fn. 345.
[348] See *supra* Chapter 4.2.3.

The Available Techniques to Determine the Substantive Law and Available Sources of Law					
Applicable Technique or Source of Law	*Amiables compositeurs*	*Voie directe*	*Voie indirecte*	*Dépeçage*	*Choice of transnational law*
Under ICC Rules	Express consent of parties required	Allowed	Allowed	Allowed	Allowed
Under CIETAC Rules & PRC Law	Allowed in the absence of a Chinese conflict rule + express consent of parties required	Not allowed	Allowed in the absence of a Chinese conflict rule	Unsettled issue	Allowed as a supplement in the absence of applicable Chinese conflict rule

The conclusions of the conducted functionalist comparison can be summarised as follows. On the one hand, the choice-of-law methodology applied in ICC arbitration allows for the arbitrators' to exercise broad discretion regarding the selection of the substantive law in the absence of the parties' instructions. On the other hand, although the CIETAC Rules do not *de jure* restrict the use of 'modern' choice-of-law methodology, the default application of the presumptory conflict rules featured by PRC law in CIETAC arbitration results in a narrow discretion of the arbitral tribunal to independently select the substantive law and thus a *de facto* prohibition of arbitrators' choice-of-law power. Consequently, the application of the Chinese choice-of-law methodology has been rightly

assessed to be an illustration of "the lowest level of the arbitrators' choice-of-law power in modern international arbitration".[349]

[349] See Chi 2011, pp. 279 – 281. Chi has also compared the application of the UNIDROIT Principles between ICC and CIETAC-administered arbitrations. According to his view, CIETAC tribunals have a tendency to neglect transnational law as a source of law. See Chi 2010, pp. 25 – 29.

5 The Choice Between ICC and CIETAC Arbitration – a Perspective of Private International Law

5.1 Significance of the Substantive Law

Before the choice between ICC and CIETAC arbitration in Sino-foreign dispute resolution is further analysed, one valid question should be answered: Does the choice of the substantive law really matter? After all, it has been argued that as the rules of contemporary business law around the world have been harmonised, the significance of the choice of the substantive law in relation to the outcome of the dispute has correspondingly decreased.[350]

While this observation might be true to a certain extent, such a thesis does not acknowledge that such cases in which there still are substantial differences in respect to competing laws continue to exist. The said discrepancies could dictate the outcome of the dispute and thus make the choice of the governing law of utmost importance to the parties. For instance, different legal systems may feature distinct solutions in relation to transfer of title or risk, rate of legal interest or procedural time limits.[351]

Most importantly, the international business community seems to perceive the choice of the substantive law to be the most important factor compared to the choice of the seat, applicable arbitration rules and arbitral institution. Whenever international business agreements are drafted, this apparently is the natural inclination: the choice of the governing law comes first and is decided by the corporate lawyers of the parties before the negotiation of the dispute resolution agreement even begins. This in turn is strongly influenced by the type of the contract and the counterparty. In other words, the parties choose the substantive law first, as this will apply throughout the contractual relationship, and the seat or the institution/rules second, as this choice will only matter if a dispute arises at a later stage.[352]

The answers of the cited questionnaire would seem to be consistent with the analysis made by practitioners familiar with issues related to private international law. For instance, Graffi has aptly noted that the possibility of disputes arising from contractual relationships is not always given much

[350] See Lowenfeld 2005, p. 177.
[351] See Ferrari – Kröll *et al.* 2010, p. 305 and Wortmann 1998, p. 99. Chinese law has been noted to feature several strict time limits in relation to limitation of claims. See Seppänen 2005b, p. 585.
[352] See International Arbitration Survey 2010, p. 8.

thought during contract negotiations. Arbitration agreements may sometimes be drafted by corporate lawyers or businesspersons who possess little or no practical experience regarding international arbitration.[353] In order to avoid uncertainty regarding the choice of *forum*, parties involved in international contracts have grown a tendency to resort to incorporating model clauses recommended by leading international arbitration institutes as part of their underlying contract.

Another reason for the absence of a choice-of-law clause may also be that the parties' have simply been unable to reach an agreement regarding the substantive law. Sometimes the parties, after a long period of negotiation, are simply not able to agree upon the content of choice-of-law clause. Instead of starting to negotiate again, the parties might prefer to leave the issue open, or to postpone the problem to the time that a dispute arises rather than not to conclude the contract.[354] As the determination of the substantive law is, however, generally regarded as a very complex task, parties have been recommended to specify the applicable law as clearly as possible.[355]

Regardless of the grounds for the absence of a valid choice-of-law clause, a substantial number of agreements that are submitted to ICC arbitration have not had a valid choice-of-law clause. Statistics indicate that in 12 per cent of ICC arbitrations conducted in 2012, the parties had not validly agreed upon the applicable law.[356]

No such statistical data seems to be available regarding CIETAC arbitration. However, it would seem appropriate to assess that this figure could be even higher in CIETAC arbitrations because the Chinese mentality of doing business tends to advocate the speedy execution of transactions at the cost of proper due diligence.[357] On the other hand, foreign companies could also contribute to the absence of a valid choice-of-law clause premised on their own 'Orientalist' prejudices.[358]

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[353] See Ferrari – Kröll *et al.* 2010, pp. 21 – 22.
[354] See Born 2009, pp. 67 and 73 – 75 and Wortmann 1998, p. 98, fn. 14.
[355] See Fouchard – Gaillard – Goldman 1999, p. 788.
[356] See ICC Statistics 2012.
[357] Antti Herlin, the chairman of the board of KONE Corporation, currently the largest Finnish enterprise conducting business in China, has publicly assessed that whereas Finnish corporate cultural norms dictate that roughly 80 per cent of the details of an agreement are clear before execution, the same figure in Chinese corporate culture would be around 20 per cent. See Herlin 2013.
[358] See Seppänen 2005b, pp. 591 – 592.

5.2 The Choice Between ICC and CIETAC Arbitration

The appropriate method to judge the success (or failure) of the ICC and CIETAC choice-of-law methodology would seem to be to inquire whether the methodology to choose the substantive law enjoys the support of the various interest groups related to international arbitration. Generally speaking, arbitration scholars tend to prefer choice-of-law methodology that allows the parties and their chosen arbitral tribunal to exercise a seemingly unlimited amount of discretion. The choice-of-law methodology embodied in the ICC Rules is a fine example of this approach.[359] Under the ICC Rules, the arbitral tribunal is provided with a wide scope of discretion although they are powerfully simple, thus enabling the arbitrators' the chance to focus on the selection of the most suitable rules of law to the merits of the dispute.[360] This is not to say that the ICC Rules would be perfect as they are. Instead, the perceived advantage of the ICC Rules is their relative simplicity and flexibility. In practice, even the most sophisticated arbitration rules will often need to be supplemented by more detailed provisions imposed by either the parties or the arbitral tribunal, e.g. the IBA Rules.[361]

The international business community has certainly approved the ICC's approach. Today, the arbitration services offered by International Chamber of Commerce are arguably perceived to be the world's most prestigious. According to a recent survey conducted by the School of International Arbitration, the ICC boasts the most distinguished private dispute resolution mechanism in the world: one half of the respondents to the survey chose the ICC as their preferred arbitration institution.[362]

On the other hand, CIETAC arbitrators themselves have claimed that the choice-of-law methodology applied in CIETAC arbitration currently complies with contemporary international arbitration practice.[363] Although the majority of (Western) arbitration scholars have abandoned the

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[359] See, for instance, Cordero-Moss 1999, p. 212 and Fouchard – Gaillard – Goldman 1999, p. 865.

[360] In Gaillard's opinion, the direct approach confers the arbitral tribunal "unfettered freedom" with regard to identifying the applicable conflict rule. See Gaillard 2004, p. 203. Should one accept the justifications for the arbitrators' wide discretion regarding the choice of the substantive law, Saarikivi suggests that the *voie directe* is a superior method to doctrines requiring a conflict of laws analysis. See Saarikivi 2008, pp. 85 – 86.

[361] See Grierson – van Hooft 2012, p. 149 and Redfern – Hunter 2009, p. 178.

[362] See International Arbitration Survey 2010. The survey was based on an unprecedented 136 questionnaire responses with further qualitative data drawn from 67 in-depth interviews. Questionnaire respondents and interviewees were general counsel and other corporate counsel from corporations across a range of industries and geographical regions, and a significant number of corporations based in emerging markets.

[363] Lu claims that "[t]he basic approach for a tribunal to determine the governing law of an arbitration is to look into the conflict rules of the seat of arbitration". See Lu 2012, pp. 313 – 314. The bulk of arbitration scholars have, however, abandoned such a point of view. See *supra* Chapter 2.

point of view represented by Lu, it is fair to admit that the use of presumptory rules does undeniably guarantee a degree of legal certainty and predictability.[364] Chi has, however, assessed that the application of the Chinese choice-of-law rules in CIETAC arbitration fits rather poorly in the context of contemporary international commercial arbitration. In his view, the use of Chinese rules of private international law in international arbitration proceedings complicates the applicable law identification process in an unduly manner, which endangers the efficiency and flexibility of the arbitration. Secondly, it confines the arbitrators' discretion to truly choose the substantive law to a few exceptional situations, which puts the arbitral tribunal in an inferior position in comparison to their international counterparts. Thirdly, as the process is established by CCL, GPCL, LAL and the SPC judicial interpretations, it is not tailored for arbitration but applies to both arbitrators and the judges. By blurring the difference between arbitration and litigation, the private nature of arbitration is not sufficiently respected.[365]

Indeed, in terms of the arbitrators' discretion to select the substantive law in the absence of party instructions, the comparison conducted *supra* in Chapter 4.3 indicates that proceedings which take place under the ICC Rules offer the arbitral tribunal far more discretion in comparison to the choice-of-law approach applied in CIETAC arbitration. In other words, the principle of party autonomy is given far more emphasis in ICC arbitration in comparison to CIETAC arbitration.

From the perspective of party autonomy, ICC arbitration thus appears as a preferable option in comparison to CIETAC arbitration.[366] Although such a statement can be considered a rule of thumb when deciding whether to opt for either of these arbitral institutions, such situations do exist when the amount of the arbitrators' discretion to identify the substantive law would appear as practically insignificant with regard to the choice between ICC and CIETAC arbitration. These exceptions can be identified in advance to extend to at least two situations, i.e. whenever:

1) the subject matter of the contract falls into the scope of application of a uniform law convention, such as the CISG; and

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[364] The objectives of achieving legal certainty and predictability were considered to be the key arguments for the extension of the closest connection rule to Chinese private international law. See Yu *et al.* 2009, p. 427. The current ambiguity regarding the existence of valid presumptory rules seems, for the time being, to remove this advantage. See *supra* Chapter 4.2.3.

[365] See Chi 2011, p. 275.

[366] Based on his experience in dealing with Chinese parties, Zimmerman has supported a such conclusion. See Zimmerman 2010, p. 23.

2) the arbitrators' choice-of-law power is subject to the limitations set by the mandatory rule of Chinese law.

To begin with, the United Nations Convention on Contracts for the International Sale of Goods ("CISG") is to be directly applied in sales contracts entered by parties whose places of business are located in different Contracting States.[367] According to UNCITRAL, a total of 80 countries have joined the CISG to date, including the People's Republic of China.[368]

Extensive judicial practice exists regarding the direct application of the CISG in China. In a dispute between a Chinese buyer and an American seller, the Supreme People's Court held that absent a valid choice-of-law clause, the CISG was applied under Article 1(1)(a) because the parties were incorporated in China and the United States, respectively, both of which are Contracting States.[369] Based on the cited judgment, it has been argued that the Chinese interpretation focuses on the place of incorporation rather than the place of business as prescribed in Article 1(1)(a).[370] Similar reasoning has been confirmedly resorted to in several published CIETAC arbitral awards and judicial practice.[371]

The PRC has made two reservations concerning the application of the CISG, the first of them being the reciprocity reservation pursuant to Article 95 of the CISG.[372] The reciprocity reservation excludes the 'indirect application' of the CISG, i.e. situations in which both of the home jurisdictions of the parties in an international sales contract have not signed the CISG. In other words, the Chinese reservation restricts the role of private international law in Sino-foreign contracts.[373] The second Chinese reservation concerns the exclusion of Article 11 of the CISG,

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[367] See CISG Art. 1(1)(a). It is, however, today a common practice in cross-border contracts that the parties decide to, either expressly or implicitly, exclude the application of the CISG. See, for instance, Johnson 2011.
[368] See http://www.uncitral.org/uncitral/en/uncitral_texts/sale_goods/1980CISG_status.html. Last visited 9th of January 2014.
[369] See Lianhe Enterprise (US) Ltd. v. Yantai Branch of Shandong Foreign Trade Co.
[370] See Xiao – Long 2008, p. 65.
[371] See CIETAC Award 1996; CIETAC Award 2002 and Minermet S.p.A Milan v. China Metallurgical Import & Export Dalian Co. and China Shipping Development Co., Ltd Tramp Co.
[372] The Chinese declaration reads as follows: "The People's Republic of China does not consider itself to be bound by subparagraph (b) of paragraph 1 of Article 1." See UN Treaty Collection. Available at https://treaties.un.org/pages/ViewDetails.aspx?src=TREATY&mtdsg_no=X-10&chapter=10&lang=en#EndDec. Last visited 30th of March 2014.
[373] See Xiao – Long 2008, p. 66 and Wang – Andersen 2004, p. 145.

which requires contracts "to be concluded in or evidenced by writing". The effect of this reservation is still a matter of dispute, and thus cannot be thoroughly discussed in this study.[374]

The mandatory application of Chinese law is of the utmost importance in the case of foreign-invested enterprises. Contemporary China is the largest recipient of foreign direct investment in the world.[375] Prior to investing in China, foreign investors are recommended obtain a thorough knowledge of relevant Chinese commercial, investment, environmental, trade and contract law, and other applicable laws.[376] As concluded *supra* in Chapter 4.2.2, the arbitral tribunal should choose to resolve all FIE-related matters on the basis of Chinese law in order to ensure the enforceability of the rendered arbitral award in the People's Republic of China. Consequently, such a conclusion effectively excludes the parties' or their chosen arbitrators' discretion to apply an otherwise applicable law as the substantive law in FIE-related matters.

Although the principle of party autonomy is an important factor regarding the choice of the arbitral institution, it is not the only one. In the case of Sino-foreign dispute resolution, it would appear that the weight put on 'extralegal' factors, such as the prejudices of both sides regarding both ICC and CIETAC arbitration, are seemingly of extraordinary significance.[377] In the end, the choice of the arbitral venue may prove to be a matter of bargaining chips. For instance, the choice of an arbitral venue could have been sacrificed in order to be able to decide the substantive law or for a lower bulk price.[378] In Zesch's view, CIETAC is often chosen as a compromise result after the underlying contract negotiations. On the one hand, foreign parties want to avoid litigation in Chinese courts. On the other hand, their Chinese business partners are uncomfortable with litigation outside China.[379] Thus, the CIETAC seems to be the closest venue to even ground.

But why not remedy this by choosing mainland China as the seat for ICC arbitrations? In practice, Sino-foreign arbitration proceedings administered by the ICC are usually seated in Hong Kong,

[374] See Xiao – Long 2008, pp. 83 – 86 and Wang – Andersen 2004, pp. 161 – 164.
[375] With regard to the choice of the entity, foreign investors have been noted to possess a tendency to opt for joint ventures instead of establishing wholly foreign-owned enterprises. This is due to the foreign investors' belief that succeeding in China requires having a well-connected Chinese partner. See Peerenboom 2002, pp. 476 – 477.
[376] See Tao 2012a, p. 111. As a result of China's accession to the World Trade Organisation in 2001, China's principal foreign investment laws have been amended. Although foreign investment to China has grown significantly as a consequence of the more liberal trade policy, China's admission to the WTO has, however, not resolved the institutional deficiencies of China's legal system. See Chen 2008, pp. 641 – 643 and Peerenboom 2002, pp. 492 – 496.
[377] See *supra* Chapter 3.
[378] See Håkansson 1999, p. 54.
[379] See Zesch 2012, p. 283.

Singapore and other Asian countries, and rarely in mainland China.[380] The principal reason for this is the requirement set by the CAL, which requires an arbitration institution to register within PRC judicial and administrative departments.[381] The ICC and other foreign arbitration institutions, however, are not registered as arbitral institutions in mainland China, and thus do not meet this requirement. In consequence, foreign-related arbitration proceedings seated in mainland China are usually administered by Chinese arbitration institutions, such as the CIETAC or the BAC.

This being said, some parties have agreed to arbitrate under the auspices of the ICC for arbitrations seated in mainland China. There has been an ongoing debate among arbitration practitioners as to whether ICC awards rendered in mainland China should be recognised as valid, and whether they can be enforced in mainland China. The Ningbo Intermediate People's Court has recognised an ICC arbitration award issued by a sole arbitrator in Beijing in 2009, but in doing so treated the award as 'non-domestic' – despite the fact that the arbitration was seated in mainland China – and based its decision to recognise the award on the New York Convention rather than on the PRC Civil Procedure Law.[382]

The cited court decision seems to represent an exception rather than the prevailing rule. Despite a willingness to support ICC arbitration seated in China seems to exist, the reasoning of the Ningbo Intermediate People's Court in reaching its conclusion has been widely questioned.[383] To date, there have been no judicial interpretations or legislative clarifications from the higher level courts to further clarify this issue. Absent such express clarification, most practitioners continue to recommend against the use of arbitration clauses providing for arbitrations with a mainland China seat that are administered by the ICC. In conclusion, although Chinese courts have taken steps in the direction, which would allow for ICC-administered arbitration in mainland China, Hess has considered it unlikely that the Chinese authorities will recognise the ability of foreign institutions to administer arbitrations seated in mainland China.[384]

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[380] For instance, the year 2012 saw 12 ICC arbitrations seated in China, of which only one was seated in mainland China and the other 11 in Hong Kong SAR. See ICC Statistics 2012.
[381] See CAL Art. 10.
[382] See Duferco S.A. v Ningbo Arts and Crafts Import and Export Co Ltd.
[383] See Hess 2010, p. 2.
[384] Ibid.

5.3 Is There a Remedy to Enhance the Arbitrators' Choice-of-Law Power in CIETAC Arbitration?

The arbitrators' low discretion to make choice-of-law decisions under the CIETAC Rules could be attempted to be improved by applying, for instance, the ICC Rules in a CIETAC-administered arbitration. Again, Chinese law does not set a *de jure* ban on the arbitrators' discretion to choose the substantive law.[385] In consequence, *voie directe* could be validly applied in CIETAC arbitration as the parties would have explicitly agreed upon it in their arbitration agreement. This could, for example, be materialised by agreeing to apply the ICC Rules in CIETAC arbitration. Such an agreement would confer the CIETAC arbitrators' the same discretion as their international counterparts.

The parties' possibility to agree upon the application of the arbitration rules of another institution or the UNCITRAL arbitration rules has been explicitly confirmed in the CIETAC Rules, which state the following:

> [w]here the parties agree to refer their dispute to CIETAC for arbitration but have agreed on a modification of these Rules or have agreed on the application of other arbitration rules, the parties' agreement shall prevail unless such agreement is inoperative or in conflict with a mandatory provision of the law as it applies to the arbitration proceedings. Where the parties have agreed on the application of other arbitration rules, CIETAC shall perform the relevant administrative duties.[386]

CIETAC arbitrators have noted the application of ICC or UNCITRAL Rules, to the extent as far as possible, to be, in fact, a fairly common practice.[387] In Lu's view, the relevant issue rather is whether the CIETAC is capable of providing the required service under other arbitration rules.[388] Because of the general Chinese reluctance to *ad hoc* arbitration, the application of the rules of an arbitration institution, such of the ICC, in CIETAC arbitration would seem like the more viable alternative.[389] Nevertheless, the direct application of the arbitration rules of other arbitration institutes is not advisable as it could conflict with the referred arbitration rules and expose the

[385] See Chi 2011, pp. 279 – 281.
[386] See CIETAC Rules Art. 4(3).
[387] See Lu 2012, p. 312.
[388] Ibid.
[389] See *supra* fn. 30.

rendered award to challenges.[390] Should the parties acknowledging the advantages still wish for the application of separate choice-of-law rules instead of a choice-of-law clause, the most amicable solution would, perhaps, be to simply agree upon the application of the *voie directe* in the parties' underlying agreement.

These observations would, however, appear to have only theoretical value. Should the parties be aware of the relative ambiguities and complexities related to the determination of the substantive law under the choice-of-law rules applied in CIETAC arbitration already during contract negotiations, it would make more sense to rather include a choice-of-law clause in the underlying contract instead of agreeing on the application of more 'modern' choice-of-law rules.[391] In consequence, the only appropriate remedy for enhance the discretion of CIETAC arbitrators regarding the determination of the substantive law would be to amend the CAL so that Chinese arbitral tribunals would, too, be mandated to apply the choice-of-law rules they deem applicable or appropriate. As noted *supra* in Chapter 2.1, this could be realised by adding a provision similar to, for instance, Article 28 of the Model Law in the CAL.[392]

5.4 Largest Risks

Premised upon the large amount of scholarly writing on the issue, the largest risk presented by relevant issues of private international law arguably is the admission of an arbitral award that does not respect the mandatory rules of Chinese law.[393]As discussed *supra* in Chapter 4.2.2, Chinese law establishes number of limits to party autonomy *inter alia* when the subject matter of the contract is related to foreign-invested enterprises. In such matters, the parties (or, in the last resort, the arbitral tribunal) should ensure that the law applied to the merits of the dispute is Chinese law. If the

[390] See Art. 1(2) of the ICC Rules, which provide that the ICC is the only institution authorised to administer ICC arbitration proceedings. In a case brought to the Singapore Court of Appeals, the issue was about whether an arbitration agreement may validly provide for one arbitral institution to administer an arbitration under the rules of another arbitral institution. The claimant's appeal was, however, dismissed. See Insigma Technology Co Ltd v. Alstom Technology Ltd**.**
[391] See Craig – Park – Paulsson 2000, p. 319; Várady – Barceló – von Mehren 1999, p. 632 and *supra* Chapter 5.1.
[392] See Lando 1991, pp. 137 – 138.
[393] Virtually all scholars or practitioners researching Chinese arbitration tend to dedicated at least a part of their attention for the status of enforcement of arbitral awards in China. See, for instance, Taylor 2013; Gu 2013; Leung 2013; Tao 2012b; Chi 2009; Cohen 2006; Seppänen 2005b, p. 586 and Peerenboom 2001.

mandatory rules of Chinese law are not respected, the arbitral tribunal risks rendering an award that is *de facto* unenforceable in Chinese courts.[394]

With regard to choice-of-law issues, the exact scope of application of the mandatory rule of Chinese law is currently ambiguous because of the abolishment of the SPC Interpretation 2007. However, it is advisable to abstain from the choice of an otherwise applicable law in all FIE-related matters. This conclusion is due to the SPC's likeliness to issue a new judicial interpretation, which could formally reinstate mandatory limits of party autonomy formerly featured in Article 8 of the SPC Interpretation 2007.[395]

Notwithstanding the compulsory application of Chinese law to FIE-related contracts, contracting parties are permitted to submit for overseas arbitration in foreign-related contractual disputes. However, the mandatory application of Chinese law in such contracts makes the discussion regarding the pros and cons of a choice-of-law methodology practically insignificant in agreements featuring a FIE as a party. In fact, it may be argued that CIETAC arbitration is in FIE-related matters a particularly favourable option in comparison to ICC arbitration. Firstly, it is likely that CIETAC arbitrators, accustomed to the mandatory requirements set by Chinese laws and regulations, are more capable than ICC arbitrators of taking the ambiguities of Chinese law – whether justified or not – into account whenever procedural decisions need to be made.[396] Secondly, a CIETAC arbitral tribunal has arguably better chances of ordering interim measures on the Chinese party than a foreign arbitral tribunal based on the newly revised Article 21 of the CIETAC Rules.[397] Thirdly, whenever negotiations for the establishment of a foreign-invested enterprise are conducted, foreign investors have been noted to experience tremendous difficulties in convincing the Chinese side to accept overseas arbitration.[398] Based on these observations, it is unsurprising to note that

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[394] Regarding the practical significance of mandatory rules or public policy of the country of enforcement in connection with the choice-of-law analysis, see *supra* fn. 345. Liukkunen has observed that the relevance of mandatory rules to international arbitration proceedings is currently growing. In correspondence with the said trend, she suggests that the role of party autonomy in international commercial arbitration might be in decline. See Liukkunen 2013, p. 203 and 217 – 222. In the author's opinion, the significance of the mandatory rules of Chinese law seem to support such a thesis.
[395] See *supra* Chapter 4.2.3.
[396] Zimmerman recommends the choice of Chinese law as the substantive law in CIETAC arbitrations as such a bargain may persuade the Chinese party to agree to have the seat of the arbitration in Hong Kong. See Zimmerman 2010, p. 24.
[397] See Lu 2012, pp. 305 – 307. Chinese courts have been noted to be reluctant to order interim relief in aid of arbitration proceedings. See Zesch 2012, p. 287.
[398] See Gu 2013, p. 79; Tao 2012a, p. 111 and Zimmerman 2010, p. 24.

disputes related to foreign direct investment into China have comprised a major part of all the foreign-related disputes submitted into CIETAC arbitration in the past.[399]

Another relevant threat for the efficient enforceability of the rendered arbitral award is posed by the possible classification of a CIETAC-administered arbitration as domestic one. Albeit a dispute featuring a Chinese party and a foreign party is unlikely to be classified as domestic,[400] the situation becomes different when the dispute features a foreign-invested enterprise and a Chinese party as the claimant and the respondent. FIEs are, under Chinese law, considered Chinese legal entities without exception.[401] Consequently, the dispute is likely to be classified as domestic and thus may be subjected to a broader review in the enforcement stage under the auspices of Chinese law.[402] Moreover, the closed-panel system of appointing arbitrators featured in CIETAC arbitration only allows for the appointment of foreign arbitrators in foreign-related arbitration proceedings. Conversely, this means that only Chinese nationals may be appointed as arbitrators in disputes featuring a FIE.[403] Needless to say, the said situation is likely to be unsatisfactory from the foreign investors' perspective.

[399] See Lu 2012, p. 302, in fn. 6.
[400] For a more thorough explanation regarding the Chinese classification of disputes, see *supra* Chapter 1.4.1.
[401] According to statistical data gathered from the CIETAC, more than 60 per cent of its domestic cases have involved FIEs. See Moser *et al.* 2007, p. 57 – 58.
[402] See *supra* Chapter 1.4.1.
[403] See CAL Art. 67 and Gu 2008, pp. 123 – 124 and 129 – 130.

6 Conclusions

The differences in the choice-of-law methodology applied in ICC and CIETAC arbitration are seemingly rooted in the paradigm struggle between the jurisdictional and delocalisational theory of international arbitration. Although most arbitration scholars, practitioners and the international business community today emphasise the delocalised and autonomous nature of international arbitration, it does not mean that the *lex arbitri* would not exist. Indeed, the boundaries according to which the parties and their chosen arbitral tribunal may exercise their autonomy continue to be, in the end, determined by national law. Although national arbitration laws have been extensively harmonised, the jurisdictions of individual states, such as the People's Republic of China, may still feature, at least from the perspective of a Western jurist, a peculiar arbitration regime.

The dichotomy of legal frameworks under which ICC- and CIETAC-administered arbitrations currently operate thus explain the discrepancies of their choice-of-law methodologies. Chinese Arbitration Law, among other issues, does not allow CIETAC-administered arbitral tribunals to exercise any discretion regarding the choice of the applicable choice-of-law rules. Therefore, it is the CAL that ultimately forces the arbitral tribunal to apply the conflict rules of the law of the PRC.

Such a choice-of-law methodology, i.e. the traditional approach, does not, however, adequately meet the needs of contemporary international commercial arbitration. The conducted functionalist comparison indicates that while the choice-of-law methodology applied in ICC arbitrations allows for an arbitral tribunal to exercise broad discretion regarding the selection of the substantive law, the default application of the presumptory conflict rules featured by PRC law in CIETAC arbitration results in a narrow discretion of the arbitral tribunal to independently select the substantive law and thus a *de facto* prohibition of arbitrators' choice-of-law power. Subsequently, CIETAC arbitrators operate in an inferior position when compared to, for instance, ICC arbitrators. Alongside this and other, perhaps even more urgent, issues, the credibility of the CIETAC to provide a rational alternative compared to, for instance, ICC arbitration is currently undermined.

Although contemporary business law around the world has now been harmonised, it does not mean that the choice of the substantive law would not be a matter of importance. In fact, the parties and/or their counsels still typically decide the substantive law before the choice of the arbitral venue and/or applicable arbitration rules. This is not to say that all agreements contain a valid choice-of-law clause regardless of recommendations to the contrary. In terms of the arbitrators' discretion to select the substantive law in the absence of party instructions, ICC arbitration offers the arbitral tribunal far more discretion in comparison to the choice-of-law rules applied in CIETAC arbitration.

In other words, the principle of party autonomy is given far more emphasis in ICC arbitration in comparison to CIETAC arbitration. In terms of party autonomy, ICC arbitration thus appears to be the preferable option in comparison to CIETAC arbitration. This being said, extralegal factors, such as the prejudices of the parties and balance of bargaining power between them, seem to be of extraordinary significance whenever arbitration clauses are drafted between Sino-foreign parties.

Despite its shortcomings, CIETAC-administered arbitration seems to be an attractive option in small-interest disputes, in which either the subject matter of the dispute or the nationality of the parties directs the arbitral tribunal to apply the law of the People's Republic of China as the substantive law. In order to ensure the effectiveness of the rendered arbitral award in Chinese courts, it is advisable to avoid the choice of an otherwise applicable law when the mandatory rules of Chinese law provide otherwise. Alas, the parties possess no effective remedies to enhance the arbitrators' choice-of-law power in CIETAC arbitration. Should they be aware of the complexities related to a choice-of-law analysis, it is more sensible to agree upon a choice-of-law clause instead of the application of a more 'modern' choice-of-law methodology.

The study has indicated that most of the problems related to arbitration in China rather stem from the inadequacy of the CAL to fit the needs of contemporary international arbitration proceedings than the CIETAC itself. Therefore, the author strongly recommends, alongside other acquainted scholars,[404] for the CCP to reconsider the reformation of the CAL so that, among others, the choice-of-law methodology applied in CIETAC arbitrations may be revised. In the light of late development, a reform of the Chinese arbitration regime, however, seems unlikely in near future. Instead, the CCP and the SPC are both seemingly committed to preserve the status quo, at least with regard to arbitration held in mainland China.[405] This might be due to the relatively large number of domestic arbitrations that a revision of Chinese arbitration would affect.[406] Therefore, it is only when the Chinese Communist Party is ready for the full-range judicial reform of Chinese arbitration when the choice-of-law methodology applied in CIETAC arbitration can be truly made to match international standards.

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[404] See Gu 2013, p. 131 and Chi 2011, pp. 279 – 281.
[405] In the author's opinion, the content of the recent SPC judicial interpretations seems to indicate that the dual-track regime is, for the time being, here to stay. See *supra* Chapter 1.4.1 regarding the SPC Interpretation 2013.
[406] See Lu 2012, pp. 299 – 300. The author considers that the Chinese Party-state is particularly reluctant to give up control with regard to its own citizens. See *supra* Chapter 3.